

**FINANCIAL LEVERAGE AND PERFORMANCE OF COMMERCIAL BANKS IN
KENYA: A CASE STUDY OF THE NATIONAL COMMERCIAL BANK OF AFRICA,
NAIROBI**

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DECLARATION

This research project is my original work and has not been presented for a degree in any other University

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This research project has been submitted with my approval as the university supervisor.

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DEDICATION

The research project is dedicated to my wife Amina and twin daughters, Aabidah and Ameirah for their tireless support during my study.

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I sincerely thank the Almighty Allah for this far he has brought me. I also wish to thank my supervisor, Prof. John Cheluget, for his helpful direction during this study process. His knowledge and support have greatly influenced the direction of this research. I thank NCBA Bank for contributing crucial information and ideas that enhanced the study. For this study to be completed successfully, the management and employees of the bank had to cooperate and support it. To the Management University of Africa family, I appreciate them for providing the first-rate academic setting and resources that made this research possible. My learning and development have been substantially aided by the institution's dedication to academic achievement.

ABSTRACT

Commercial banks' performance is largely determined by their financial leverage. This study investigated the effect of financial leverage on the performance of Kenya's NCBA Bank. It focused on credit risk management practices, the cost of debt, capital structure decisions, and interest rate volatility, all of which influenced the bank's profitability, liquidity, and overall stability. The purpose of the study was to examine how credit risk management, cost of debt, capital structure, and interest rates affect financial performance. The research was anchored on three key financial theories: the Trade-Off Theory, the Pecking Order Theory, and the Agency Theory. A descriptive research design was adopted, and data were collected through a structured questionnaire administered to a sample of 148 employees, of which 136 responses were properly completed and analysed. Descriptive statistics showed that respondents generally agreed that credit risk management, cost of debt, and interest rate were key drivers of financial performance. Regression analysis revealed that credit risk management ($\beta = 0.355$, $p = 0.001$) and interest rate ($\beta = 0.688$, $p = 0.028$) had a significant positive influence on financial performance, while cost of debt ($\beta = -0.479$, $p = 0.039$) had a significant negative effect. Capital structure, however, had no statistically significant effect ($\beta = 0.018$, $p = 0.959$). The overall model was statistically significant ($F = 5.675$, $p = 0.000$) with an R-squared value of 0.148, indicating that the four independent variables explained 14.8% of the variation in financial performance at NCBA Bank. The study recommended that NCBA Bank strengthen its credit risk management frameworks, optimize the cost of borrowing through strategic debt sourcing, and enhance interest rate risk management to improve profitability. Although capital structure was not a significant predictor in this context, it was suggested that it be regularly reviewed to ensure financial stability. Future research was recommended to expand the study to include multiple banks for generalizability, consider additional financial and operational variables, adopt longitudinal designs, and possibly use mixed methods to uncover deeper insights into leverage-performance dynamics. These efforts would help build a broader and more nuanced understanding of financial performance in Kenya's banking sector.

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ACRONYMS AND ABBREVIATIONS

BCBS	Basel Committee on Banking Supervision
CBK	Central Bank of Kenya
LCR	Liquidity Coverage Ratio
LDR	Loan-to-Deposit Ratio
MENA	Middle Eastern and North African
NCBA	National Commercial Bank Of Africa
NACOSTI	National Commission For Science, Technology and Innovation
ANOVA	Analysis Of Variance
NIM	Net Interest Margin
NPLs	Non-Performing Loans
ROA	Return on Assets
ROE	Return on Equity

OPERATIONAL DEFINITION OF TERMS

Capital Structure	Amount of debt and equity a bank utilizes to finance its assets and activities.
Cost of Debt	The total expense incurred by a bank in servicing its debt, including interest payments, transaction costs, and other financing fees.
Credit Risk Management	A set of strategies and processes that banks implement to assess, control, and minimize the likelihood of financial loss due to borrowers defaulting on their obligations.
Financial Leverage	The process that shows how much debt a business is employing to fund its activities.
Financial Performance	This is how effectively a company uses its resources and runs its business to produce income and profit over a specific time frame. It is a gauge of a business's financial well-being and capacity to meet financial goals.
Interest Rate Volatility	The amount of interest rate volatility during a specific time period that impacts lending rates, borrowing costs, and total bank profitability
Regulatory Compliance	The adherence of a bank to financial laws, industry regulations, and supervisory requirements set by regulatory bodies such as the (CBK)

CHAPTER ONE

INTRODUCTION

1.0 Introduction

The chapter provides a description of main theme of this study from global, African, regional and local perspective. It also outlines the issue statement, research goals, the importance of the study, its scope, and a chapter summary.

1.1 Background of the Study

Financial leverage is essential in banking sector, as it involves strategic use of borrowed funds to enhance returns on investment. By leveraging debt, banks can expand their operational capacity, increase their lending potential, and strengthen their competitive position in the market (Zelalem, 2020). This approach allows financial institutions to maximize profitability while maintaining a relatively lower equity base. However, while financial leverage can be beneficial, excessive reliance on debt can expose banks to significant risks. High leverage levels may lead to liquidity challenges, making it difficult for a bank to meet its short-term obligations (Angima, Miroga, & Otinga, 2022). Effective risk management, regulatory compliance, and prudent financial planning are necessary to ensure that leverage is used optimally without compromising the institution's long-term sustainability (Enria, & Woods, 2022).

The concept of financial leverage is widely studied in global financial markets. According to Modigliani and Miller (1958), under ideal market conditions, financial leverage does not affect a firm's value. However, in reality, capital structure decisions significantly impact banking performance due to market imperfections such as taxes, bankruptcy costs, and asymmetric information (Berger & Bouwman, 2020). In developed economies, banks utilize leverage to optimize returns on equity while managing risks through regulatory frameworks such as Basel III, which imposes capital adequacy requirements to ensure financial stability (BIS, 2019). Studies in the U.S. and European banking sectors indicate that excessive leverage contributed to the 2008 financial crisis by exposing banks to liquidity and insolvency risks (Admati & Hellwig, 2020). In contrast, well-capitalized banks with controlled leverage ratios tend to have higher resilience and profitability.

In Africa, financial leverage plays a dual role: enabling expansion while posing systemic risks. The banking sector in Africa is characterized by high-interest margins, underdeveloped

capital markets, and significant reliance on short-term debt financing (Beck & Cull, 2020). Many African banks face regulatory pressures to maintain leverage within acceptable limits, but challenges such as limited access to long-term funding and high non-performing loans persist. Empirical studies suggest that financial leverage positively influences bank performance when managed prudently. A study by Naceur and Omran (2020) on Middle Eastern and North African banks found that higher leverage increases return on equity but may also heighten financial vulnerability. The risk-return trade-off is particularly evident in countries with weak regulatory enforcement and macroeconomic instability.

According to a study by Murikwa (2020), Kenyan commercial banks' financial performance and leverage were positively correlated. Likewise, Njoroge and Mugambi's (2021) study made clear that, good risk management techniques are necessary. Financial leverage is essential to bank operations in Kenya, which has one of the most vibrant banking sectors in East Africa. The Central Bank of Kenya enforces capital adequacy regulations under the Basel framework to ensure financial stability (CBK, 2022). Kenyan banks, including NCBA Bank, leverage debt financing to expand credit facilities and enhance profitability. The bank's financial statements indicate a strong capital base, with a leverage ratio that aligns with regulatory requirements. NCBA has expanded its asset base through credit offerings, digital banking solutions, and corporate lending. However, like other Kenyan banks, NCBA faces risks associated with leverage, such as loan defaults and economic downturns (NCBA Annual Report, 2023).

NCBA Bank, a prominent Kenyan commercial bank, has experienced substantial growth, partly due to strategic financial leverage practices. The bank's 2023 financial statements indicate a 15.3% increase in customer deposits and an 18.6% growth in assets, reflecting its leverage strategies. Financial leverage is a double-edged sword in the banking sector, affecting profitability, risk exposure, and financial stability. Globally, leverage management is critical for bank performance, while in Africa, it facilitates expansion despite regulatory and economic challenges. In Kenya, NCBA Bank has leveraged debt strategically, but it must continuously assess its risk exposure to maintain financial health. Future research should explore the impact of digital transformation on leverage strategies in African banking (Murikwa, 2020).

1.1.1 Credit Risk Management Practices

Identification, evaluation and mitigation of prospective losses are all part of credit risk management, if borrowers fail to meet their financial obligations. Effective practices include the use of credit scoring models, setting collateral requirements, and continuous monitoring of credit exposures. To fully assess and manage credit risk, financial institutions frequently use frameworks such as the CAMEL grading system (McKinsey & Company, 2023). Rising interest rates, high inflation, and geopolitical tensions are some of the factors that have contributed to the increased volatility of the financial environment in recent years. The significance of strong credit risk management procedures has been highlighted by these circumstances. It is recommended that financial institutions review and improve their credit risk management strategies in order to successfully handle economic uncertainty.

Monitoring loan portfolios, evaluating borrower creditworthiness, and putting policies in place to reduce possible losses from non-performing loans are all made easier by efficient credit risk management. Because they are better able to handle bad debts and preserve asset quality, organizations with strong credit risk management frameworks typically report stronger profitability and financial stability (Njanike, 2020). Interest income, a major source of income for many financial institutions, is protected when default rates are decreased through the use of appropriate risk assessment tools, prompt loan monitoring, and adherence to lending standards.

According to Owusu-Antwi and Antwi (2020), by raising loan default rates and eroding investor trust, inadequate credit risk management can seriously jeopardize an institution's financial stability. Ineffective credit risk management can result in a large number of non-performing loans (NPLs), which deplete capital reserves and necessitate increased provisioning. This reduces the bank's capacity to make additional loans, which limits revenue production and may result in liquidity issues. Financial performance may also be further strained by regulatory penalties for subpar credit management techniques. Because they handle credit-related risks proactively, companies that invest in ongoing employee training, use sophisticated credit scoring algorithms, and implement strict credit appraisal procedures typically outperform rivals over the long term.

1.1.2 Cost of Debt

According to a study by Murikwa (2020), factors influencing the cost of debt include prevailing interest rates, the company's creditworthiness, and broader economic conditions. By lowering interest costs, a reduced cost of debt can improve a business's financial performance. Conversely, a higher cost of debt can strain a company's finances, especially if it leads to increased leverage and potential financial distress. Companies must carefully manage their debt levels and strive to maintain favourable credit ratings to secure debt at reasonable costs. Effective debt management strategies are essential to balance the benefits of leverage against the risks associated with high debt costs.

According to Musiega et al. (2020), because it affects a company's capital structure and profitability, the cost of debt has a big impact on its financial success. By lowering interest costs, a reduced cost of debt can improve financial performance by raising net income and return on equity. Businesses that are able to get loans at advantageous interest rates frequently demonstrate better financial performance because interest payments are tax deductible, hence reducing the total cost of capital. As a result, businesses have more money to invest in lucrative projects, grow their business, or increase shareholder value. Thus, a company's competitive edge in the market can be strengthened and financial performance optimized with a strategic balance between debt and equity and a controllable cost of debt.

A high cost of debt can have a detrimental effect on financial performance by making interest payments more onerous, decreasing profitability, and possibly causing financial trouble. Businesses that incur high interest costs as a result of unfavourable loan terms or low credit ratings are more likely to experience lower profitability and less financial flexibility, claim Chepkorir and Moronge (2020). This could make them more susceptible to economic shocks or downturns and limit their capacity to reinvest earnings into expansion prospects. Furthermore, excessive debt that has significant servicing costs can undermine overall financial sustainability, lower stock values, and erode investor confidence. Thus, maintaining sound financial performance requires controlling the cost of debt through sensible borrowing choices and efficient creditworthiness techniques.

1.1.3 Capital Structure

Various theories offer frameworks for comprehending how various capital arrangements can impact a company's valuation and cost of capital. The significance of incorporating risk

management into capital structure choices has been emphasized by recent studies. As an example, the interaction between operational hedging and financial flexibility can significantly impact a firm's value. Understanding these dynamics helps companies make informed decisions about leveraging and financing strategies to enhance shareholder value.

A well-designed capital structure can optimize shareholder value, improve profitability, and reduce the total cost of capital. Businesses that balance debt and equity are better able to take use of the advantages of debt financing, like tax breaks for interest payments, while lowering the dangers of using too much leverage, claim Mwangi and Birundu (2020). Businesses can increase returns on equity and assets thanks to this balance, which enhances their overall financial performance. Because it demonstrates prudent financial management and strategic decision-making, a well-structured capital mix also increases investor confidence.

Otieno and Nyang'au (2020) revealed that, due to higher interest commitments and the possibility of financial trouble, an unbalanced capital structure-especially one with excessive debt-can have a detrimental impact on financial performance. Businesses with high debt ratios may experience liquidity issues, lower profitability, and less financial flexibility, particularly during recessions or times of low sales. Growth and profitability may be hampered by the temptation to make fixed interest payments, which might take funds away from worthwhile ventures. Furthermore, excessive financial leverage can harm a company's credit rating and result in erratic profitability, which raises the cost of borrowing money in the future. Thus, preserving long-term financial performance and competitiveness requires a carefully thought-out capital structure.

1.1.4 Interest Rate Volatility

Changes in interest rates over time that significantly affect borrowers and financial institutions are the interest rate volatility, in order to preserve their financial stability, banks and insurers must effectively manage interest rate risk. To protect against unfavourable changes in interest rates, strategies like gap analysis, duration analysis, and the usage of derivatives are frequently used. Due to a number of economic causes, interest rate volatility has increased in the financial markets in recent years. This volatility poses challenges for financial institutions in managing their interest rate risk exposures effectively. Implementing robust risk management frameworks is essential to navigate such volatile environments and ensure financial stability.

The financial performance of businesses is greatly impacted by interest rate volatility, particularly those in interest-sensitive industries like banking, insurance, and real estate. Interest rate fluctuations have an impact on profitability margins, investment choices, and borrowing prices. Unexpected increases in interest rates result in higher debt servicing costs, which lower net income and put pressure on cash flows. This situation is especially difficult for businesses that have a lot of variable-rate debt. Karuiru and Muturi (2020) claim that abrupt increases in interest rates have a detrimental impact on business performance by raising financial expenses, restricting access to reasonably priced borrowing, and deterring long-term investment planning. In variable rate settings, businesses with inadequate hedging strategies may face increased financial risk, decreased profitability, and diminished competitiveness.

However, by reducing borrowing costs and promoting capital investments, falling interest rates can improve financial performance. Excessive volatility, however, can result in cautious or less-than-ideal investment behaviour and add uncertainty into financial planning. Interest rate changes affect financial institutions' interest revenue and net interest margins, which raise their risk exposure, claim Otieno and Odhiambo (2020). For example, when rates fluctuate quickly, banks that rely on the difference between lending and deposit rates may find their profits compressed. Furthermore, rate volatility may affect asset-liability matching, affect financial instrument valuation, and need higher risk management expenses. In order to preserve financial stability and enhance long-term financial performance in the face of interest rate volatility, efficient interest rate risk management techniques-such as the use of interest rate swaps or other derivatives-are crucial.

1.1.5 Financial Performance

A company's capacity to turn a profit and provide value for its shareholders is gauged by its financial performance. By examining these measures, one may gain knowledge about the business's overall financial health, profitability, and operational effectiveness. A company's ability to effectively manage risks like credit and interest rate variations are some of the elements that affect its financial success. To improve financial performance and guarantee long-term sustainability, it is crucial to put best practices in risk management into practice and to keep the right ratio of debt to equity financing (Darno and Gelatan, 2025).

Finding, evaluating, and reducing the possibility that a borrower or counterparty won't fulfil their responsibilities are all part of effective credit risk management. Robust practices in this area are essential for maintaining financial stability and performance. Establishing a suitable credit risk environment and maintaining appropriate credit administration processes to manage credit risk effectively is essential. In recent years, economic volatility has heightened the need for sound credit risk management. Factors such as rising interest rates, high inflation, and geopolitical tensions have deepened uncertainty for bank credit exposures (Enria, & Woods, 2022).

The cost of credit, encompassing interest rates and associated fees, directly impacts a company's borrowing expenses and profitability. Higher credit costs can strain cash flows, reducing net income and hindering financial performance. Conversely, access to affordable credit can facilitate expansion and operational efficiency. Effective credit risk management can lead to more favourable borrowing terms, thereby enhancing financial performance (IOSR Journals, 2022). Returns can be maximized and the cost of capital reduced with the right balance. Nonetheless, having too much debt raises financial risk and can result in financial difficulties (Capital One, 2023). Hedging and diversification are two risk management techniques that have been shown to affect a company's capital structure choices.

Interest rate changes have the potential to impact financial performance by affecting borrowing costs as well as investment returns. Organizations with significant debt may experience increased interest expenses during periods of rising rates, while those with interest-sensitive assets might see variable returns (Basel Committee on Banking Supervision, 2025). Effective interest rate risk management is essential to stabilize finances in volatile markets. Hedging techniques, for instance, can lessen the effect that changes in interest rates have on a business's bottom line. In conclusion, there is a complicated and important interaction between capital structure, interest rate volatility, cost of credit, and credit risk management techniques. Proactively managing these factors puts an organization in a better position to improve its financial performance and attain long-term sustainability.

1.2 Statement of the Problem

While financial leverage drives growth and profitability, excessive use can lead to financial instability. NCBA Bank's consistent use of debt financing has supported its expansion, but the sustainability of these practices is uncertain amid evolving economic conditions. The intricate connection between bank performance and financial leverage has been brought to

light by recent studies. This implies that, higher debt levels may burden banks with increased interest obligations, potentially diminishing returns. Additionally, a study examining the moderating role of artificial intelligence (AI) found that while financial leverage negatively affects firm performance, the integration of AI can mitigate these adverse effects, leading to improved ROE (Darno, and Gelatan, 2025).

Despite prior contributions, important gaps remain. Chukwu and Efanga (2025) do not disaggregate findings for the banking sector or explore how leverage interacts with bank-specific indicators (ROA, ROE, liquidity), and they do not account for NCBA Bank's unique market position and recent strategic initiatives. Broader corporate-sector studies on financial leverage focus on non-bank firms and therefore overlook banking-specific features such as regulatory capital requirements, liquidity management and interest-rate exposure, limiting their applicability to commercial banks. Furthermore, empirical work on Kenyan banks typically relies on short cross-sectional samples and single profitability measures (usually ROA), which constrains causal inference and ignores longer-term and multidimensional performance outcomes. Given changing economic conditions, it is therefore essential to investigate how NCBA Bank's use of debt financing affects multiple performance indicators (ROA, ROE and liquidity ratios), and how this relationship is conditioned by the bank's strategic initiatives and the Kenyan regulatory and macroeconomic environment. This study will close those gaps by using bank-specific measures, a longitudinal design, and explicit consideration of NCBA's market positioning, providing policymakers, regulators and financial institutions with better evidence on the sustainability of debt financing in Kenyan commercial banks.

1.3 Objectives of the Study

1.3.1 General Objective

To determine the effect of financial leverage on financial performance of commercial banks in Kenya with a focus on The National Commercial Bank of Africa Headquarters Nairobi

1.3.2 Specific Objectives

- i. To assess the effect of credit risk management on financial performance of the NCBA Bank Kenya Plc
- ii. To analyse the relationship between cost of debt and financial performance of the NCBA Bank Kenya Plc.

- iii. To assess the effect of capital structure on financial performance of the NCBA Bank Kenya Plc.
- iv. To examine the effect of interest rate volatility on financial performance of the NCBA Bank Kenya Plc.

1.4 Research Questions

- i. How does credit risk management affect financial performance of the NCBA Bank Kenya Plc?
- ii. To what extent does the cost of debt affect financial performance of the NCBA Bank Kenya Plc?
- iii. What is the effect of capital structure on financial performance of the NCBA Bank Kenya Plc?
- iv. How does interest rate volatility affect financial performance of the NCBA Bank Kenya Plc?

1.5 Significance of the Study

By offering empirical data on the link between financial leverage and Kenyan commercial banks' performance-with a focus on NCBA Bank-this study will contribute to the corpus of knowledge in academia. There is a knowledge gap about how leverage works in developing countries like Kenya because the majority of the current research on financial leverage focuses on industrialized economies. This study will close this gap in the Kenyan banking industry by analysing actual data.

The present scholars and future researchers who study banking and financial management would also benefit from knowing how leverage impacts important performance metrics. The study's conclusions can be used as a guide for future research, encouraging more investigations into bank profitability, risk management, and financial leverage in Kenya and throughout Africa.

The analysis will assist in determining the ideal debt load that maintains financial stability while optimizing profitability. This result will assist in directing capital structure decisions and provide risk management techniques to lessen financial hardship and liquidity issues related to excessive leverage. Provide benchmarking insights by comparing NCBA's leverage strategy with industry peers, helping the bank stay competitive, and support strategic

decision-making on whether to increase or decrease leverage depending on prevailing economic conditions, regulatory frameworks and market dynamic. By applying these insights, NCBA Bank can enhance its financial sustainability and shareholder value.

The study's findings can assist regulators in, refining banking regulations to balance financial innovation with stability, ensuring that banks do not over-leverage, revising leverage limits by determining whether current capital adequacy requirements sufficiently mitigate systemic risks, enhancing risk management frameworks, guiding banks on best practices in capital allocation and debt utilization, and developing stress testing guidelines, ensuring banks can withstand economic downturns without facing liquidity crises. By using the study's recommendations, CBK can strengthen the banking regulatory framework, fostering a stable and resilient financial system in Kenya.

Investors and stakeholders in NCBA Bank, will gain a clearer understanding of assessing risk-return trade-offs, ensuring informed investment decisions based on leverage levels and profitability trends, identify potential red flags related to excessive leverage that may lead to financial distress or insolvency, gauge financial stability by evaluating how NCBA Bank balances debt and equity financing and predict future performance trends, aiding in long-term investment planning and stock valuation.

1.6 Scope of the Study

The study focused on NCBA Bank's financial leverage practices and their effect on performance indicators such as ROA, ROE, and liquidity ratios. The study was conducted between January to October 2025, analysing financial statements, risk management strategies, and macroeconomic factors affecting financial leverage decisions. The study was conducted at the NCBA Bank's headquarters, Nairobi Kenya.

1.7 Chapter Summary

By giving background information on financial leverage and its function in commercial banking, this chapter has introduced the subject. The problem statement, study goals, questions, significance, and scope have all been described. The following chapter will examine pertinent literature with an emphasis on conceptual models, empirical research, and theoretical frameworks pertaining to financial leverage and bank performance.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

The chapter discussed key theory on which the study was pegged on and any other three theories that supported the main theory. The theories were considered based on their relevance to the study objectives, empirical review to help on the identification of the research gaps, the conceptual framework, and operationalization of variables and chapter summary.

2.1 Theoretical Literature review

Understanding connection between bank performance and financial leverage requires a strong theoretical basis. The Trade-Off Theory, which describes how businesses balance debt and equity to enhance performance while reducing financial distress, serves as the foundation for this investigation. The anchor theory is further supported by three auxiliary theories: the Pecking Order Theory, Agency Theory, and Modern Portfolio Theory. These theories shed light on various factors influencing financial performance, including interest rate volatility, capital structure, cost of debt, and credit risk management.

2.1.1 Trade-Off Theory

Kraus and Litzenberger's (1973) Trade-Off Theory is still a mainstay of corporate finance, especially when it comes to describing how businesses choose their best capital structures. According to the idea, businesses weigh the possible costs of financial distress, agency conflicts, and bankruptcy risks against the advantages of debt financing, such as tax shielding and higher returns on equity. The theory basically says that when the marginal benefit of debt is equal to its marginal cost, there is an optimal capital structure.

A major critique of this theory is that it assumes firms have precise knowledge of their risk-return trade-offs and can easily determine an optimal leverage level. In reality, firms especially in dynamic financial environments like Kenya's banking sector face uncertainty and regulatory constraints that complicate such optimization. Additionally, the theory may not fully account for behavioral factors, market imperfections, or managerial risk aversion that influences financing decisions (Maxwell, 2020).

The theory relevance to this study lies in its direct connection to the financial leverage decisions of commercial banks such as NCBA Bank. As banks strive to balance profitability and solvency, they must evaluate the advantages of using debt to expand credit facilities while managing the risks of over-leverage. This study applied the theory to assess how credit risk management, cost of debt, capital structure, and interest rate volatility influence the bank's financial performance. For instance, NCBA Bank's ability to maintain an optimal leverage ratio determines its capacity to lend sustainably without exposing itself to insolvency risks (Enria & Woods, 2022).

Financial institutions also use the Trade-Off Theory to control credit risk, making sure that lending policies meet capital adequacy and risk tolerance requirements. Because excessive leverage increases exposure to default risk, sound credit risk management techniques including portfolio diversification, stress testing, and risk-based lending are crucial. In order to avoid systemic crises, the Central Bank of Kenya mandates that banks balance their exposure to risk and debt use through prudential standards (Basel Committee on Banking Supervision, 2025).

Another component that is consistent with the Trade-Off Theory is the cost of debt. Despite the tax benefits of debt, excessive borrowing increased the risk of default and, consequently, borrowing costs. Financially stable banks maintain optimal leverage levels where the cost of debt does not erode its benefits. Empirical findings suggest that banks that manage leverage efficiently tend to record stronger financial sustainability and competitive advantage (Chukwu & Efanga, 2025). This aligns with NCBA Bank's financial strategy, where cost-effective debt management enhances profitability and stability.

Finally, interest rate volatility influences how effectively banks apply the Trade-Off Theory. Variations in interest rates affect borrowing costs, loan pricing, and net interest margins, thereby impacting overall financial performance. Research indicates that institutions with adaptable capital structures are better positioned to absorb rate shocks and maintain financial resilience (Darno & Gelatan, 2025). Therefore, this theory provided a theoretical foundation for understanding how NCBA Bank balances the use of debt for growth against the risks associated with financial instability.

2.1.2 Pecking Order Theory

A Myers and Majluf's (1984) Pecking Order Theory offers an alternate explanation for financial leverage choices. According to the hypothesis, businesses would rather use retained earnings for internal financing than debt or stock for external financing. Businesses are more likely to use debt than to issue fresh equity when external financing becomes necessary. This preference stems from the fact that internal funds don't have issuance costs, whereas external financing could come with higher transaction costs and knowledge asymmetry. This idea is especially pertinent to commercial banks since regulatory capital requirements and liquidity considerations have an impact on financial decisions. Therefore, before turning to external borrowing, banks typically prioritize retained earnings to finance loan portfolios and asset growth (McKinsey & Company, 2023).

A notable critique of this theory is that it assumes firms always have sufficient internal funds and ignores the possibility that firms may strategically use debt for tax advantages or to signal financial strength. Moreover, in highly regulated sectors such as banking, institutions often face mandatory capital adequacy thresholds that compel them to use both internal and external sources of financing. The theory also overlooks the influence of macroeconomic conditions and investor expectations on financing behavior, which can lead to deviations from the idealized pecking order (Zelalem, 2020).

The relevance of this theory on this study lies in its emphasis on internal financing and its implications for the key determinants of financial performance, credit risk management, cost of debt, capital structure, and interest rate volatility. In terms of credit risk management, banks that rely more on internal funds are less exposed to default risk and can maintain stronger credit portfolios. This is because they reduce dependency on external borrowing and thereby minimize excessive leverage. Empirical evidence shows that financial institutions adopting prudent earnings retention policies report lower default rates and enhanced loan portfolio quality, strengthening overall financial stability (IOSR Journals, 2022).

The cost of debt is another area where the Pecking Order Theory is applicable. According to this framework, banks that prioritize internal financing can maintain stronger credit ratings and negotiate favorable borrowing terms. Conversely, overreliance on external debt leads to higher financing costs due to perceived risk exposure. Studies reveal that institutions aligning their financing strategies with the Pecking Order Theory often record improved financial

performance owing to reduced dependence on costly external borrowing (Njoroge & Mugambi, 2021).

Furthermore, institutions adhering to this approach maintain conservative leverage ratios, emphasizing financial resilience over aggressive expansion. This conservative financing structure ensures solvency during economic downturns and minimizes exposure to financial distress. Evidence indicates that firms with lower leverage and greater reliance on internal capital tend to achieve superior long-term profitability and operational stability (Murikwa, 2017).

In relation to this study, the Pecking Order Theory provided a theoretical basis for understanding how NCBA Bank's financing preferences influenced its financial performance. The study demonstrated that the bank's tendency to utilize retained earnings before external borrowing aligns with the theory's postulates, thereby shaping its credit risk management practices, cost of debt, and capital structure decisions in pursuit of sustainable profitability (Wambua & Otieno, 2024).

2.1.3 Agency Theory

Conflicts The Agency Theory, developed by Jensen and Meckling (1976), examines the conflicts of interest that arise between principals (shareholders) and agents (managers) in organizations. The theory postulates that such conflicts occur when managers, who control day-to-day operations, pursue personal goals such as maximizing short-term profits or managerial benefits at the expense of shareholders' long-term wealth. Within the banking sector, these conflicts are particularly significant due to the complex nature of financial leverage and risk-taking behavior. When managers engage in excessive borrowing or risky lending to boost short-term returns, they expose banks to increased credit risk and potential financial instability. To minimize these conflicts, effective governance mechanisms, regulatory oversight, and incentive alignment systems are essential in ensuring that managerial decisions reflect the best interests of shareholders (Angima, & Otinga, 2022).

A key critique of the Agency Theory is that it assumes rational behavior and clearly defined relationships between managers and shareholders, which may not always exist in practice. It also overlooks external factors such as regulatory interventions, market competition, and macroeconomic pressures that influence managerial decision-making. Moreover, the cost of monitoring and controlling managerial behavior known as *agency cost* can be substantial, particularly in large, complex financial institutions. Despite these limitations, the theory

remains highly relevant in explaining how governance and financial policies influence organizational performance.

This theory relates to this study lies in its application to leverage management and financial performance within commercial banks such as NCBA Bank. In terms of credit risk management, the theory helps explain how managerial decisions regarding loan approvals and debt exposure can either enhance or undermine financial stability. High leverage may incentivize managers to engage in risky lending practices to increase returns, thereby elevating credit risk. Conversely, strong governance structures such as independent risk management committees and internal audit systems help reduce agency conflicts and maintain prudent lending practices (McKinsey & Company, 2023).

Regarding the cost of debt, Agency Theory suggests that higher agency costs may increase borrowing costs because creditors perceive the institution as riskier when managerial interests are misaligned with shareholder goals. Similar to this, agency concerns impact capital structure decisions since businesses need to figure out the best debt and equity ratio to reduce agency expenses and maximize company value. Sound governance mechanisms ensure that managers select financing options that enhance profitability without exposing the firm to excessive risk (Poot, 2020).

In relation to interest rate volatility, Agency Theory provides insight into how managerial decision-making under fluctuating economic conditions affects a bank's financial performance. Managers driven by short-term incentives may increase leverage during low-interest periods, heightening vulnerability when rates rise. Therefore, NCBA Bank's adherence to sound governance practices and responsible leverage management aligns with the Agency Theory's emphasis on minimizing conflicts of interest to enhance financial performance (Nyambura & Kibet, 2024).

2.1.4 Modern Portfolio Theory

Harry Markowitz created the Modern Portfolio Theory (MPT) in 1952, and it highlights diversification as a key idea for risk management and return optimization. According to the hypothesis, by diversifying over a range of assets, investors can create efficient portfolios that optimize projected returns for a specific degree of risk. The basic idea is that by combining assets with imperfectly correlated returns, a portfolio's overall risk can be decreased. In the context of the banking industry, this theory is highly relevant in guiding institutions on how to manage credit risk and interest rate volatility through diversification strategies. By

spreading lending portfolios across various sectors, borrower categories, and geographical regions, banks can reduce their vulnerability to market fluctuations and economic downturns, thereby achieving greater financial stability (Basel Committee on Banking Supervision, 2025).

A key critique of the Modern Portfolio Theory is that it relies heavily on the assumptions of rational investors, stable correlations, and normally distributed returns, conditions that rarely hold true in real-world financial markets. Moreover, the theory does not fully account for systemic risks, sudden market shocks, or behavioural biases that can influence investment and lending decisions. In the banking context, diversification alone may not eliminate credit and liquidity risks, especially when economic shocks affect multiple sectors simultaneously. Therefore, while MPT provides a useful foundation for risk management, it should be complemented by more dynamic and adaptive financial models that account for changing market conditions (Smith & Zhao, 2024).

The relevance of the Modern Portfolio Theory to this study lies in its application to the management of credit risk and interest rate volatility, which are critical components of financial performance. Banks such as NCBA Bank apply diversification principles by distributing their lending portfolios across multiple sectors to mitigate default risk and stabilize income streams. This approach helps protect the bank's profitability and liquidity during periods of market turbulence. Empirical evidence supports the idea that financial institutions with well-diversified credit portfolios tend to have lower default rates and enhanced financial resilience (Chukwu & Efanga, 2025).

Furthermore, the Modern Portfolio Theory complements other financial frameworks in explaining how banks make leverage-related decisions. While the Trade-Off Theory focuses on balancing the costs and benefits of debt and the Pecking Order Theory emphasizes financing preferences, MPT highlights how risk diversification supports sustainable financial performance. Together, these theories provide an integrated framework for understanding how NCBA Bank manages leverage, credit exposure, cost of debt, and interest rate fluctuations to achieve financial stability and long-term profitability within Kenya's dynamic banking sector (Otieno & Odhiambo, 2020).

2.2 Empirical Literature Review

Empirical literature provides evidence-based insights into how financial leverage and its related components influence the performance of commercial banks across different contexts.

Unlike theoretical perspectives, which offer conceptual frameworks, empirical studies present findings derived from actual data and statistical analysis. This section reviews previous research conducted locally and internationally on variables such as credit risk management, cost of debt, capital structure, and interest rate volatility, and their combined effect on financial performance. The review helps to identify existing research gaps, highlight consistencies or contradictions among prior findings, and establish how the current study builds upon and contributes to the existing body of knowledge on financial leverage and banking performance (Smith, Brown & Taylor, 2022).

2.2.1 Credit Risk Management and Financial Performance

Recent Recent empirical studies have increasingly examined how credit risk management influences financial performance across different sectors. Maintaining profitability, reducing credit losses, and guaranteeing business sustainability all depend on efficient credit risk management procedures. However, the nature of this relationship often varies depending on industry context, governance structure, and technological adoption, creating a growing need for context-specific research to deepen understanding of credit risk management effectiveness (Smith & Zhao, 2024).

Noja et al. (2021) carried out an empirical investigation among European financial service firms to examine how board composition relates to financial performance and risk management disclosure. Drawing on data from 144 companies across 25 European countries obtained from the 2020 Thomson Reuters Eikon database, and employing Gaussian Graphical Models (GGMs) alongside Structural Equation Modeling (SEM), the study revealed that board features, particularly size, gender diversity, and the presence of a two-tier governance structure positively influenced risk management disclosure and led to better financial performance. These findings highlighted that strong corporate governance structures play a vital role in supporting effective credit risk management and overall financial success. However, the research primarily focused on financial institutions in developed economies, leaving a gap regarding how similar governance and credit risk management mechanisms function in developing countries such as Kenya, where organizational and regulatory environments differ considerably (Noja et al., 2021).

Poot (2020) examined the role of CRM and Credit and Collection Management Practices (CCMP) in promoting sustainability and profitability within private higher education institutions. Statistical methods were applied to assess four main CCMP dimensions

coordination, leadership, organization and personnel, and planning and their relationship with CRM components such as credit risk control and collection policies. Findings revealed a moderately positive relationship between well-structured CCMP frameworks and institutional profitability, indicating that efficient credit and collection practices enhance financial performance. Nonetheless, this study was confined to education sector, which limits its applicability to other industries such as logistics or manufacturing that face different credit risk dynamics and operational challenges (Poot, 2020).

Effective credit risk control is strongly associated with increased profitability, according to Maxwell's (2021) investigation on the relationship between credit risk management tactics and financial performance. According to the survey, organizations who implemented strict credit risk management procedures saw improvements in risk mitigation and financial stability. However, it also observed that not all credit risk management practices yielded significant financial benefits, suggesting that their effectiveness may vary across different contexts and organizational structures. This highlights a research gap on the moderating role of contextual factors such as organizational culture, technology use, and regulatory frameworks in shaping the effectiveness of credit risk management practices across sectors (Maxwell, 2021).

In another study, Aziakpono and Sanga (2023) performed a bibliometric and systematic literature review on FinTech and SME financing from 2008 to 2022. Their analysis indicated that empirical research on FinTech-related credit risk management practices has expanded significantly since 2018, primarily employing quantitative methods based on survey and platform data. The study revealed that FinTech innovations have improved credit risk management processes by enhancing data precision, minimizing transaction costs, and reducing information asymmetry. Additionally, FinTech adoption has streamlined lending procedures from credit screening to repayment, thereby improving efficiency and financial inclusion. However, rapid technological adoption has also introduced new risks such as data privacy issues and cyber threats. The research did not empirically test how FinTech-driven credit risk management practices directly impact financial performance, especially in emerging economies like Kenya where digital finance ecosystems are still maturing (Aziakpono & Sanga, 2023).

Overall, the reviewed studies consistently affirm that effective credit risk management contributes positively to financial performance by enhancing profitability, stability, and

sustainability. However, most existing research has been conducted in developed economies or within the financial and educational sectors, leaving limited evidence on how credit risk management practices influence financial outcomes in logistics companies operating in developing markets. Therefore, the purpose of this study is to close these gaps by investigating the relationship between credit risk management methods and the financial performance of Kenyan logistics companies, offering a contextualized and sector-specific knowledge of the efficacy of credit risk management.

2.2.2 Cost of Debt and Financial Performance

A major subject in contemporary corporate finance, the dynamic relationship between a firm's cost of debt and its financial performance has been better understood thanks to recent empirical studies. The effective rate at which a business repays borrowed money is known as the cost of debt, and it has a big impact on long-term financial stability, capital structure, and profitability. Prior studies have examined various determinants of debt costs, including firm-specific characteristics, macroeconomic conditions, and regulatory frameworks. However, notable research gaps persist in understanding how the cost of debt interacts with firm performance across different sectors and economic contexts. Furthermore, the literature remains limited in integrating emerging dimensions such as environmental, social and governance factors and corporate governance practices into analyses of debt cost determinants (Otieno, 2024).

Businesses with good ESG credentials typically have lower borrowing costs because lenders view them as less hazardous and more sustainable borrowers, according to Wang and Chen's (2023) investigation on the relationship between ESG performance and loan costs. Companies with robust ESG ratings typically benefit from favourable loan terms and reduced interest rates due to perceived lower default risks. Conversely, Smith et al. (2022) noted that firms heavily investing in ESG activities may encounter higher debt costs, particularly when such initiatives involve uncertain or long-term financial payoffs. These contradictory findings suggest that the influence of ESG performance on debt costs is not uniform and may depend on industry characteristics and the maturity of ESG integration in lending decisions. Thus, a key research gap exists in empirically validating how ESG adoption shapes debt financing outcomes in developing economies, where sustainability reporting and ESG compliance are still evolving (Wang & Chen, 2023; Smith et al., 2022).

By affecting managerial responsibility and investor trust, corporate governance also has a significant impact on the cost of debt. According to Johnson and Li (2021), companies with robust governance structures which include independent boards, efficient oversight, and open disclosure procedures are more likely to be able to obtain financing at reduced interest rates. Similarly, Nguyen and Tran (2023) observed that diversified ownership structures and gender-diverse boards enhance investor trust, leading to lower borrowing costs. However, governance mechanisms operate differently across institutional environments. Existing studies primarily focus on firms in developed markets with established governance norms, leaving a gap in understanding how variations in governance quality influence debt costs in emerging markets like Kenya, where corporate governance standards are still consolidating (Johnson & Li, 2021; Nguyen & Tran, 2023).

Capital structure and leverage ratios have also been identified as major determinants of financial performance and debt costs. Baker and Wurgler (2021) emphasized that an optimal debt level enhances firm value by exploiting tax shields and financing profitable projects, consistent with the trade-off and pecking order theories. Miller and Modigliani (2023) further demonstrated that moderate leverage can support growth by reducing the weighted average cost of capital. However, excessive reliance on debt increases financial distress risk and undermines profitability, as supported by Kumar and Singh (2024). Despite these insights, existing literature offers limited empirical evidence on the optimal leverage threshold across different industries and macroeconomic cycles, creating a research gap in identifying context-specific debt levels that maximize firm performance (Baker & Wurgler, 2021; Miller & Modigliani, 2023; Kumar & Singh, 2024).

The role of agency costs in determining the cost of debt has also attracted scholarly attention. Jensen and Meckling (2022) argued that agency conflicts where managers prioritize personal objectives over shareholder interests can lead to inefficient financing decisions and higher borrowing costs. Lenders often respond to such risks by imposing stricter lending conditions or higher interest premiums. While the link between agency costs and the cost of debt is well-documented, existing studies lack longitudinal analyses that capture how governance reforms and incentive mechanisms evolve to mitigate these agency problems over time (Jensen & Meckling, 2022). Therefore, a dynamic methodology should be used in future research to examine how ownership structure, business size, and macroeconomic factors modify the relationship between loan costs and financial performance across industries.

In summary, empirical studies underscore that the cost of debt significantly affects financial performance through its influence on profitability, capital structure, and firm sustainability. However, gaps remain regarding the contextual determinants of debt costs, particularly in developing economies where governance practices, financial regulations, and market maturity differ from those in developed nations. By examining the impact of debt costs on Kenyan commercial banks' financial performance with a particular emphasis on NCBA Bank, this study aims to close these gaps and provide context-driven insights into the effectiveness of debt financing.

2.2.3 Capital Structure and Financial Performance

Profitability, risk exposure, and overall firm value are all significantly influenced by a company's capital structure, or the ratio of debt to equity funding. Conventional financial theories, such as the Trade-Off Theory and the Modigliani and Miller framework, have long served as a guide for understanding how businesses balance debt and equity to maximize value. However, as the corporate environment changes, additional aspects like non-financial resources, financial digital transformation, and environmental, social, and governance (ESG) concerns have become important considerations when deciding on capital structure. There are still a lot of unanswered questions about how these contemporary factors affect financial performance in various industrial and economic contexts, despite a wealth of research on capital structure determinants (Owusu-Antwi & Antwi, 2020).

The integration of ESG considerations into capital structure decisions has become increasingly significant in recent years. Firms demonstrating strong ESG performance often appear as lower-risk investments, attracting favorable financing terms and investor confidence. Wang and Li (2023) found that organizations with robust ESG policies tend to experience reduced capital costs due to improved investor trust and regulatory incentives that reward sustainable practices. Conversely, Jones et al. (2022) argued that heavy investments in ESG initiatives may impose additional financial burdens, negatively impacting short-term profitability. These contradictory findings highlight that while ESG-driven firms may access cheaper capital, the extent of ESG's long-term effect on financial performance is unclear. This creates a research gap on the mechanisms through which ESG adoption influences firms' leverage ratios and cost of capital, particularly in developing economies where ESG implementation is still emerging (Wang & Li, 2023; Jones et al., 2022).

The rise of financial digital transformation has also reshaped how firms approach capital structure management. Digital technologies improve financial transparency, reduce transaction costs, and enhance risk assessment accuracy. Smith and Zhao (2024) observed that firms leveraging digital innovations, such as block-chain and fintech platforms, often enjoy greater access to alternative financing channels, including decentralized finance (DeFi) and digital lending platforms. These advancements reduce information asymmetry and improve capital allocation efficiency. However, most existing studies focus on the operational benefits of digital transformation rather than its influence on financing mix and leverage decisions. The limited empirical evidence on how digitalization affects firms' capital structure choices and long-term financial sustainability presents a key research gap that future studies should address across different regulatory and industrial contexts.

Non-financial resources (NFRs), including organizational culture, employee motivation, and stakeholder relationships, have recently attracted scholarly attention for their indirect influence on financial outcomes. Kumar and Singh (2023) emphasized that firms with strong internal cultures and stakeholder trust often demonstrate greater financial resilience and lower borrowing costs. Intangible assets such as corporate reputation and employee commitment enhance lender confidence, enabling firms to secure debt financing on favorable terms. Nevertheless, research remains scarce on how NFRs directly affect capital structure decisions and interact with financial metrics such as profitability and leverage (Kumar & Singh, 2023). The limited exploration of these intangible determinants restricts a comprehensive understanding of how both tangible and intangible assets jointly influence financial strategy.

The existing empirical studies affirm that capital structure decisions significantly influence financial performance through their effects on profitability, liquidity, and firm stability. However, contemporary determinants such as ESG adoption, digital transformation, and non-financial resources remain underexplored in capital structure literature. In order to fill these gaps, this study examined how these new factors influence capital structure choices and financial performance in the Kenyan banking industry, with a particular emphasis on NCBA Bank. Such an approach will contribute to a broader and more context-sensitive understanding of how modern business dynamics redefine capital structure optimization for sustainable financial performance.

2.2.4 Interest Rate and Financial Performance

Interest rate dynamics have long been recognized as a critical determinant of financial performance across banking institutions, corporate firms, and the broader economy. Numerous studies have examined how fluctuations in interest rates influence profitability, lending behavior, and financial stability. However, a notable research gap persists in understanding the long-term implications of unconventional monetary policies particularly negative interest rate policies on financial institutions. While existing research such as that by Altavilla, Boucinha, and Peydró (2021) has concentrated on short-term effects in traditional banking models, limited empirical evidence exists on how prolonged exposure to near-zero or negative interest rates affects financial stability and risk-taking behaviors. This study, therefore explored how interest rate fluctuations affect financial performance within emerging market contexts, where institutional and regulatory frameworks differ significantly from those of advanced economies.

The results of previous studies on how negative interest rate environments affect bank profitability and risk-taking are inconclusive. Some academics contend that banks adjust by diversifying their revenue streams through fees and commissions, while others contend that lower interest rates compress banks' net interest margins and weaken profitability (Buehler, Kaiser, & Jaeger, 2021). However, the long-term implications of NIRPs on banks' risk-taking behavior, particularly in developing economies, remain underexplored. Studies by Heider, Saidi, and Schepens (2021) reveal that banks facing negative rates often increase lending to riskier borrowers to maintain returns, heightening the potential for financial instability. This gap underscores the need for further research to determine whether prolonged exposure to unconventional interest rate regimes encourages excessive risk-taking among financial institutions in emerging markets. The study filled this gap by empirically examining how sustained interest rate changes influence both profitability and stability in developing financial systems.

While many studies on interest rate effects focus on large corporations and banks, small and medium-sized enterprises (SMEs) remain underrepresented in empirical analyses (Beck, Degryse, De Haas, & Van Horen, 2022). SMEs are particularly vulnerable to interest rate fluctuations due to their dependence on external financing and limited access to capital markets. Despite this vulnerability, few studies have examined how interest rate regimes affect SMEs' investment decisions, cash flow management, and overall financial

performance, especially in developing economies. Jiménez, Ongena and Saurina (2022) note that monetary policies aimed at stabilizing financial markets often neglect credit constraints facing SMEs. Addressing this gap, the present study will analyze the degree to which interest rate changes affect SMEs' access to finance and growth prospects in emerging markets, contributing to a more inclusive understanding of financial performance across firm sizes.

Microfinance institutions have also been largely overlooked in studies examining interest rate effects. Existing literature highlights that narrowing interest rate spreads, often driven by external monetary policies, can undermine MFIs' profitability and their capacity to serve low-income clients (Nguyen & Boateng, 2021). However, much of this evidence is based on isolated case studies, with limited comparative empirical research exploring how varying interest rate conditions affect MFIs' long-term sustainability. This study bridged this gap by investigating how interest rate fluctuations affects MFIs' financial performance, offering policy insights on how to balance profitability and social objectives under changing monetary conditions.

Furthermore, although financial institutions employ a range of strategies to mitigate interest rate risk, empirical evidence regarding the effectiveness of these strategies remains scarce (Paligorova & Santos, 2022). Most prior research has focused on large multinational banks with advanced risk management systems, overlooking smaller financial institutions and those in developing countries where risk management capacities are limited. Consequently, there is insufficient understanding of how financial institutions with varying resource levels manage exposure to interest rate volatility. By assessing the efficacy of various interest rate risk management strategies and their effects on financial stability and performance, especially in emerging financial markets, the current study filled this knowledge vacuum.

The reviewed literature reveals several key research gaps: limited understanding of long-term NIRP effects on financial institutions in emerging economies, insufficient focus on SMEs' financial responses to interest rate volatility, lack of comprehensive evidence on MFIs' resilience to changing interest rate spreads, and inadequate exploration of interest rate risk management effectiveness in less developed banking systems. By filling in these gaps, the current study will improve our understanding of the relationship between interest rates and financial performance and offer insightful information to investors, financial managers, and policymakers who want to improve stability and sustainability in dynamic economic situations.

2.2.5 Financial Performance

Financial performance has been extensively analyzed in recent years, with growing scholarly attention on the influence of digital finance integration, technological innovation, macroeconomic factors, and regional economic dynamics. Zhang and Qi (2023) found that while digital finance enhances competitiveness and financial inclusion, it simultaneously exposes banks to higher levels of operational and credit risk. Similarly, McKinsey & Company (2023) highlighted that financial institutions leveraging emerging technologies such as artificial intelligence, big data, and block-chain report improved financial performance due to enhanced efficiency and data-driven decision-making. However, these benefits are contingent upon the presence of strong governance and risk management frameworks. Despite these insights, there remains a research gap regarding how developing economies particularly in Sub-Saharan Africa can optimize digital financial adoption while mitigating the associated risks. This study bridged this gap by assessing how technological adoption and innovation affect financial performance in context of developing banking systems like Kenya's.

The World Bank (2023) emphasized the importance of effective central bank communication in maintaining financial market stability and mitigating systemic risks. In the Kenyan context, the Kenya Bankers Association (2023) reported that the country's banking sector has shown resilience amid global economic shocks, largely attributed to innovation and customer-focused strategies. This aligns with findings by Karanja (2023), who established that financial innovations have positively influenced the profitability of Kenyan commercial banks. Nonetheless, the study also noted that high regulatory compliance costs and growing cyber-security threats undermine these benefits. The present study addressed this gap by evaluating the balance between innovation-driven profitability and compliance-related costs within Kenyan financial institutions.

Technological advancements continue to reshape the global banking landscape, driving efficiency but also introducing new vulnerabilities. McKinsey & Company (2023) observed that automation and artificial intelligence-based customer engagement tools have enabled global banks to reduce operational costs and enhance service delivery, leading to improved profitability. However, excessive reliance on digital transformation without corresponding regulatory adaptation can generate systemic risks, such as cyber-security breaches and market instability. In Kenya, Karanja (2023) found that banks that failed to invest in digital

technologies experienced slower growth compared to their technologically adaptive counterparts. Notwithstanding these conclusions, there is still a dearth of empirical data regarding the long-term financial viability of digital transformation plans, especially in developing nations where legal frameworks are still developing. By examining the ways in which digital transformation affects Kenyan commercial banks' short- and long-term financial performance, this study aims to close this gap.

The rise of private credit markets and fintech start-ups has further intensified competition in the global financial sector. The Financial Times (2025) reported that private lenders are increasingly challenging the traditional dominance of commercial banks by offering flexible credit solutions and technology-driven platforms. While this increased competition fosters innovation, it also pressures banks to lower interest margins, which may negatively affect profitability. Despite these competitive threats, commercial banks continue to hold strategic advantages through customer trust, regulatory protection, and diversified service portfolios. Nevertheless, the literature lacks comprehensive empirical analysis of how intensified fintech competition affects financial performance in emerging economies. The current study will therefore examine how the growing influence of fintech and private lenders shapes the performance, resilience, and market positioning of Kenyan commercial banks.

In summary, existing literature reveals that digital finance integration, technological innovation, competitive market forces, and macroeconomic stability are key drivers of financial performance in the banking sector. However, notable research gaps persist particularly regarding how emerging market banks can sustainably manage the trade-offs between innovation, compliance, and profitability. The long-term effects of fintech disruptions, cyber-security risks, and regulatory constraints on financial performance remain underexplored, especially within Kenya's evolving financial ecosystem. By addressing these gaps, the current study will deepen understanding of how banks in developing economies can enhance financial performance through strategic adaptation, technological advancement, and effective governance frameworks.

2.3 Summary and Research Gaps

Table 1: Summary and Research Gaps

Author / Year	Area of Study	Study Findings	Methodology	Focus of the current study	Research Gaps
Noja et al. (2021)	Board Characteristics and Risk Management in Financial Services	Optimal board size, gender diversity and strong governance improve financial performance and risk disclosure. Effective risk management structures lead to better profitability.	Structural equation Modelling and network analysis using secondary data from 144 European financial service companies.	Examining financial leverage on NCBA Bank's financial performance, with a focus on governance and risk management.	Limited studies on how governance structures, such as board diversity and independence, impact financial leverage strategies in Kenyan banks.
Poot (2020)	Credit Risk Management in Higher Education Institutions	Effective credit risk management, including proper planning, organization, and monitoring, improves financial stability. Strong collection policies enhance profitability.	Descriptive research design with statistical analysis, including correlation tests and ANOVA on private HEIs in the Philippines.	Impact of credit risk management on NCBA Bank's financial performance, focusing on loan portfolio quality and risk mitigation strategies.	The study focuses on educational institutions, not banks, creating a gap in banking-specific CRM analysis. More research is needed on CRM effectiveness in commercial banks.

Author / Year	Area of Study	Study Findings	Methodology	Focus of the current study	Research Gaps
Wang & Chen (2023)	ESG and Cost of Debt	Firms with strong ESG credentials enjoy lower debt costs due to reduced risk perception by lenders. ESG-focused firms attract better financing terms.	Panel data analysis of global firms' ESG performance and debt costs.	Evaluating the cost of debt on NCBA's performance, considering factors like ESG integration and risk perception.	ESG's role in influencing financial leverage in Kenyan banks remains underexplored. More research is needed on how ESG affects debt structuring in commercial banks.
Darno & Gelatan (2025)	Financial Leverage and Bank Profitability	Financial leverage negatively affects profitability (ROA and ROE) unless moderated by artificial intelligence (AI). AI-driven risk management improves bank stability.	Quantitative analysis of banking sector financial data from 2020-2022, using regression models.	Financial leverage's effect on NCBA Bank's financial indicators, with a focus on risk management strategies.	The moderating role of AI in financial leverage strategies is understudied in Kenya. More empirical studies are needed on AI-driven financial risk management in the banking sector.

Author / Year	Area of Study	Study Findings	Methodology	Focus of the current study	Research Gaps
Chukwu & Efanga (2025)	Financial Leverage in Nigerian Industrial Firms	High financial leverage increases firm risk but can enhance profitability when managed well. Firms with excessive leverage struggle with liquidity issues.	Empirical analysis using firm-level financial data from Nigerian industrial companies.	Examining NCBA Bank's leverage impact on profitability, with a focus on liquidity risk and debt management.	The study focuses on industrial firms, not banks, leading to a contextual research gap. There is a need for sector-specific research on leverage in Kenyan banks.
Murikwa (2017)	Leverage and Financial Performance of Kenyan Banks	A positive relationship exists between financial leverage and bank performance when properly managed. However, excessive leverage can reduce profitability due to high interest expenses.	Empirical study using financial data from Nairobi Securities Exchange-listed commercial banks.	Investigating how NCBA Bank's leverage strategy influences financial stability and performance.	Existing research does not explore how leverage affects different financial performance indicators, such as liquidity ratios and capital adequacy.

Author / Year	Area of Study	Study Findings	Methodology	Focus of the current study	Research Gaps
Poot (2020)	Credit Risk Management in Higher Education Institutions	Effective credit risk management, including proper planning, organization, and monitoring, improves financial stability. Strong collection policies enhance profitability.	Descriptive research design with statistical analysis, including correlation tests and ANOVA on private HEIs in the Philippines.	Impact of credit risk management on NCBA Bank's financial performance, focusing on loan portfolio quality and risk mitigation strategies.	The study focuses on educational institutions, not banks, creating a gap in banking-specific CRM analysis. More study is needed on CRM effectiveness in commercial banks.
Zhang & Qi (2023)	Digital Finance and Bank Performance	Digital inclusive finance enhances competitiveness but increases risk exposure in commercial banks.	Empirical analysis of Chinese banks using financial performance data.	Examining how digital banking affects financial performance in commercial banks.	Limited research on how digital finance impacts banks in African markets, including Kenya.
World Bank (2023)	Macroeconomic Factors and Banking Sector Performance	Global economic downturns influence bank stability and risk exposure. Stronger regulations help sustain financial performance.	Macroeconomic analysis using financial market data.	Studying the relationship between economic policies and financial resilience in Kenyan banks.	Lack of region-specific studies on economic downturns and their direct impact on Kenya's banking sector.

Author / Year	Area of Study	Study Findings	Methodology	Focus of the current study	Research Gaps
Kenya Bankers Association (2023)	State of Banking in Kenya	Kenyan banks remain resilient due to innovation and strategic management. Digital banking boosts profitability.	Industry report analysing financial statements and trends among Kenyan banks.	Evaluating the impact of digital banking innovations on Kenyan commercial banks.	More research needed on long-term sustainability of digital banking in Kenya's financial sector.
Financial Times (2025)	Private Credit Markets and Banking	The rise of private lending firms increases competition, forcing banks to innovate to maintain profitability.	Industry analysis of private credit and traditional banking models.	Investigating the competitive dynamics between private lenders and traditional banks in Kenya.	Limited studies on how commercial banks can adapt to the rise of fintech-driven lending.

2.4 Conceptual Framework

The structure, focus, and guiding principles of a study are outlined in this framework, which acts as a fundamental research instrument. It highlights the importance of the subject being studied by synthesizing prior research and existing theories to frame on-going studies (EBSCO, 2024). A conceptual framework can be visual, often represented through graphs or charts, or narrative, incorporating detailed descriptions and organized points to enhance clarity. A well-developed conceptual framework helps researchers establish relationships between variables, define research scope, and guide data analysis.

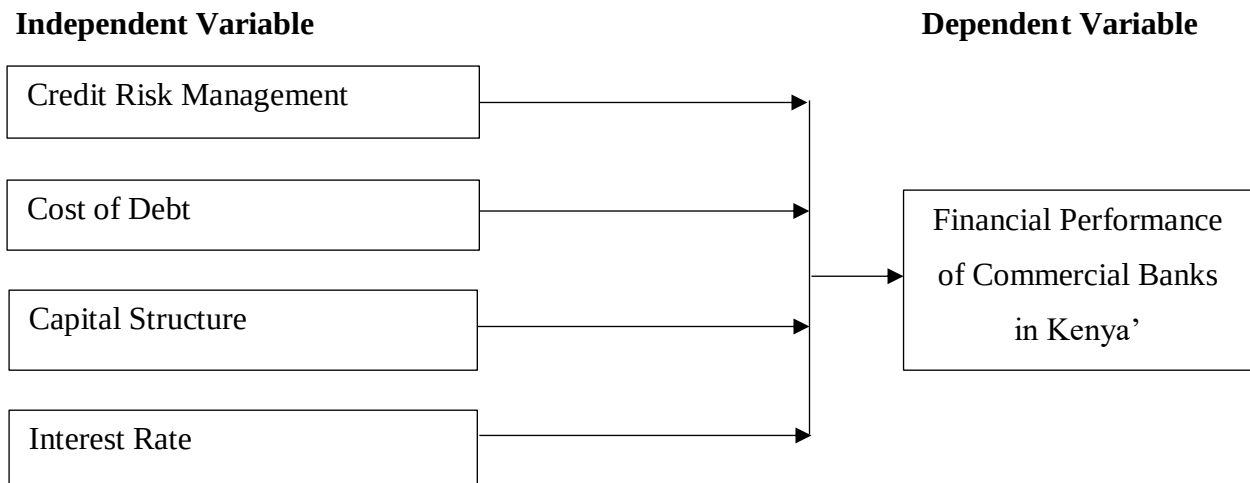


Figure 1: Conceptual Framework

2.5 Operationalization of variables

This involves identifying key variables, determining appropriate indicators, and selecting measurement scales that accurately capture the intended phenomena. This process also facilitates replication and comparison of findings across different studies, strengthening the credibility of the research. Effective operationalization ensures clarity in research methodology, allowing for precise interpretation of relationships between independent, dependent, and moderating variables.

Table 2: Operationalization of variables

Research Object	Variable Type	Indicators	Measurement Scale	Tools of Analysis
To assess how commercial banks' financial performance is affected by credit risk management	Independent	Non-performing loan ratio, loan repayment rate, loan default rate, credit risk exposure, loan loss provision ratio	Ratio Scale	Descriptive statistics, Correlation analysis, Multiple regression

Research Object	Variable Type	Indicators	Measurement Scale	Tools of Analysis
Impact of debt costs on commercial banks' financial performance	Independent	Weighted average cost of capital interest coverage ratio, average borrowing rate,	Ration scale	Descriptive Statistics and Regression analysis
To assess the impact of capital structure on financial performance of commercial banks	Independent	Debt-to-equity ratio, capital adequacy ratio, total debt to total assets ratio, long-term debt ratio, retain earnings to total capital	Ration scale	Correlation analysis, Multiple regression
To examine the effect of interest rate volatility on financial performance of commercial banks	Independent	Central Bank policy rate fluctuations, treasury bill rate movements, loan interest rate variability, inflation rate, interbank lending rate	Ratio scale	Time analysis, descriptive statistics, Regression analysis
To determine the financial performance of commercial banks	Dependent	Return on assets, return on equity, net interest margin, liquidity ratio, cost-to-income ratio	Ration scale	Trend analysis, Descriptive statistics, Regression analysis

2.6 Chapter Summary

Chapter two is a very critical chapter in the development of a research proposal or research project as it give the theories on which study is pegged on, the literature review that gives the researcher insight on the identification of research gaps and room for critique. The conceptual work that demonstrated the link of study variables, the operationalization of the variables, and the chapter's conclusion are all covered in this chapter.

CHAPTER THREE

RESEARCH DESIGN AND METHODOLOGY

3.0 Introduction

This chapter covers type of research design, research tool or instrument that enhance the data collection process. It also contains research instrument, data collection procedure, data processing, and data presentation. The chapter also addressed the chapter summary.

3.1 Research design

Research design outlined how information was gathered and guided every stage of the research process. It involved carefully selecting participants, determining where the research would take place, and choosing the most appropriate methods for collecting data to answer the specific research questions (Turner & Malik, 2024). It also served as a critical link between what the researchers intended to find out and how the answers were uncovered in practice. A descriptive research design applied focused on providing a clear and structured understanding of the target population or phenomenon. This approach utilized various methods to investigate one or more variables in depth. While it did not establish causal relationships, the descriptive research design highlighted possible associations or trends among variables, providing a valuable foundation for future research to explore these patterns more thoroughly (Turner & Malik, 2024).

3.2 Target Population

This represented the entire group of individuals about whom the researcher aimed to draw conclusions based on the study's outcomes. It served as the broader context from which insights were generalized. According to Bennett and Osoro (2024), the accessible population is the specific, reachable segment of this larger group that the researcher could practically involve in the study. In this research, the focus was on all 234 employees of NCBA.

Table 3 Target Population

Category	Frequency	Percentage
Finance Department	70	29.9
Asset Finance Department	55	23.6
Trade Finance Department	60	25.6
Investment Banking Department	49	20.9
Total	234	100.0

Source; NCBA (2025)

3.3 Sample and Sampling Technique

The systematic process of selecting particular people or groups to take part in a research from a wider population is known as sampling. By examining a well selected subgroup, this procedure enables researchers to make significant inferences about the larger population (Patel and Owino, 2024). To select the sample for the investigation, stratified random sampling was used. This approach ensures that everyone has an equal chance of being selected while taking into account the different demographic groups. Stratified sampling enhances representativeness by splitting the population into discrete groups, or strata, and then choosing participants at random from each group, as Kimani and Reyes (2025) describe. This reduces sampling error and guarantees that the findings fairly reflect each department.

Staff at NCBA Bank is therefore categorized into four strata based on their departments, as outlined in the sample size table. The research uses a well-known formula introduced by statistician Taro Yamane in determining sample size. Although originally developed in 1967, Yamane's formula remains relevant today for determining efficient and representative sample sizes, especially when researchers need to balance accuracy with resource constraints.

The formula is as follows;

Yamane formula is stated as $n = N / (1 + N(e)^2)$

Where: n = Sample Size, N = Population Size, e = Level of Precision

The level of precision is taken as 0.1.

$$n = \frac{234}{1 + 234(0.05)^2}$$

Sample Zise = 148

Table 3: Sample Size

Department	Sample Size	Percentage
Finance Department	45	30.4
Asset Finance Department	35	23.6
Trade Finance Department	38	25.7
Investment Banking Department	30	20.3
Total	148	100

3.4 Data collection Instrument

According to Kimani and Wanjiru (2025), a questionnaire that was used served as a systematic instrument for gathering data by presenting participants with a predefined set of questions aimed at obtaining statistically meaningful insights on the topic under investigation. As highlighted by Otieno (2024), questionnaires proved particularly effective for exploring intangible elements such as employees' perceptions, values, motivations, and attitudes areas that are often difficult to assess through direct observation. In addition to their analytical value, questionnaires offered several logistical advantages: they enabled the researcher to reach a broader respondent base, ensured respondent convenience by allowing completion at a preferred time, and enhanced the overall efficiency of data collection. The questionnaire comprised of participants' demographic data the study's four main variables interest rate, capital structure, cost of debt, and credit risk management.

3.5 Pilot Study

Before the main data collection process began, the research instrument underwent a pilot test to ensure its effectiveness and reliability. According to Nyambura and Kibet (2024), piloting is an essential step in research in which the questionnaire is tested on a smaller group that closely reflects the characteristics of the actual target population. This process helped evaluate whether the questions were clear, relevant, and capable of capturing the intended data. To ensure the instrument was dependable, the pilot test involved fifteen staff members from NCBA Bank. This number represented approximately 10% of the anticipated total sample size, in line with the recommendations of Muthoni and Karani (2025), who emphasize the importance of using a representative fraction of the sample to identify potential flaws in the design and structure of research tools. The final data analysis did not include the pilot group's results. Rather, by pointing out ambiguities, repetitions, or items that did not adequately support the goals of the study, the information acquired during this phase assisted in improving the questionnaire. Furthermore, the pilot study gave the researcher a chance to become acquainted with the procedure for gathering data, make any necessary modifications, and verify that the research tools accurately measured the variables being studied.

3.5.1 Validity of the Instrument

This refers to how accurately the conclusions drawn from data reflect the subject of the study. As highlighted by Kamau and Wambui (2024), validity ensures that the results of the research truly represent the concepts being investigated. Authenticity, as described by

Kiplagat and Mutua (2025), is similarly concerned with the accuracy of data in representing the topic at hand. Construct validity was evaluated in this study to see if the research tool actually assesses the theoretical idea it is intended to evaluate. This process shall involve comparing the new instrument against previously validated tools that measure the same variables.

The supervisor and other research professionals evaluated both the face validity and content validity of the questionnaire. The review process included an examination of the content, sequence, format, organization, and practical applicability of the questions and instructions. Additionally, feedback from the pilot respondents was considered, and necessary adjustments were made to the questionnaire before it was distributed to the full participant group at NCBA Bank, Headquarters, Nairobi.

3.5.2 Reliability of Research Instruments

This referred to the consistency of the results that an instrument produced across multiple tests. According to Wambua and Otieno (2024), assessing reliability is critical, as consistently reliable instruments yield accurate and dependable data over time. The dependability of the data collection instruments was assessed for this study using an internal consistency technique. A Cronbach's alpha value greater than 0.7 suggested that the instrument was adequately dependable, as suggested by Njoroge and Mwangi (2025)

Using the pilot study's early data and a 95% confidence interval, the researcher computed the Cronbach's Alpha Coefficient. Version 26 of SPSS was utilized to calculate the Cronbach's alpha coefficient after the data from the pilot phase was input into a statistical software program. A Cronbach's alpha score of more than 0.7 indicated that the questionnaire was deemed reliable for use in the primary study without the need for any changes.

3.6 Data Collection Procedure

The respondents were provided with an official letter from the Management University of Africa introducing the researcher and outlining the objectives and scope of the study. In addition, permission to collect data was obtained from NACOSTI, and an official letter from the organization facilitated this authorization process. The data collection was conducted in person at NCBA Bank, with direct interaction between the researcher and the participants. The researcher, assisted by a research assistant, distributed the surveys to the participants.

Respondents were given a four-day period to complete the questionnaires, after which they were collected for analysis.

3.7 Data Analysis and Presentation

Data analysis referred to the process of systematically organizing and structuring the collected data to draw meaningful conclusions that were easy to interpret and communicate (Johnson & Smith, 2024). Since this study was descriptive in nature, frequency distributions and percentage calculations were used to summarize the data, with the aid of SPSS software (version 28). Correlation analysis was used to determine the direction and strength of the relationships between the study's variables. To investigate the connections between variables, a correlation matrix was made. A perfect positive or negative association between the variables was represented by a correlation coefficient of ± 1.0 , while no relationship was indicated by a value of zero. Interpretation was based on values ranging from 0 (no relationship) to 1.0 (perfect relationship). To investigate the connections between the variables, regression analysis was also performed.

3.8 Ethical Consideration

3.8.1 Informed Consent

One essential element of ethical research was informed consent. Before they started taking part, participants were fully informed about the nature and goal of the study. They received thorough and understandable information regarding the goals of the study, the methods used, and any possible advantages or disadvantages. They were able to choose whether or not to participate after being given this information. Additionally, participants were told that they would not be penalized if they left the study at any point. To make sure that participants understood their rights and gave their voluntary consent, consent was sought in writing.

3.8.2 Voluntary Participation

In this study, participation was completely optional. Participants were made aware that they were under no obligation to participate and that their choice would not affect their personal or professional circumstances. The study emphasized that respondents could withdraw at any point without any repercussions, ensuring that no undue pressure was placed on any individual to participate. This commitment to voluntary participation ensured that the research process respected the autonomy and freedom of choice of all participants.

3.8.3 Confidentiality

Strict confidentiality was maintained throughout the study. All information gathered from participants was securely stored, ensuring the protection of sensitive and private data. Participants' names remained anonymous, and neither the final analysis nor the report contained any identifying information. Any information provided during the study was not shared with unauthorized parties and was used solely for research purposes. Participants were also assured that their responses would not be linked to them in any way, safeguarding their privacy and guaranteeing the confidentiality of their participation.

3.9 Chapter Summary

This research study chapter covered the research design and methodology used by the investigator during the investigation. The sample strategy, data collection tools, data collection procedures, analysis, and, lastly, ethical considerations are other topics discussed in this part.

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSION

4.0 Introduction

This chapter presents the results of data analysis, interpretation, and presentation of the findings of the study. It begins by outlining the response rate, followed by a summary of the respondents' demographic characteristics to provide context to the data. The chapter then explores the descriptive statistics of each of the study variables, credit risk management, cost of debt, capital structure, interest rate, and financial performance, using means and standard deviations to summarize patterns in the responses.

Additionally, Cronbach's Alpha is used to assess the internal consistency of the questionnaire items and confirm the trustworthiness of the data collection tool. This chapter also covers regression analysis, which examines the relationship between the independent and dependent variables and provides statistical evidence of their influence on financial performance. Finally, the findings are compared to the published empirical literature in order to validate or contrast them. This chapter aims to address the research questions and test the hypotheses derived from the data analysis.

4.1 Presentation of Research Findings

The results and comments of the output data from SPSS version 28 were given. The results came from the validity and reliability evaluation of the data that was conducted during the pilot research. Additionally, the research variable and its impact on the independent variable were discussed in the section.

4.1.1 Reliability and Validity test Result

Table 4: Reliability and Validity Result

Indicator	Cronbach's Alpha	No. of Item Tested
Credit Risk Management	0.623	5
Cost of Debt	0.706	5
Capital Structure	0.630	5
Interest Rate	0.692	5
Financial Performance	0.709	5

The reliability of the research instrument was assessed using Cronbach's Alpha, a statistical measure used to evaluate the internal consistency of questionnaire items. This analysis was

essential in determining whether the items within each construct reliably measured the intended variables. The results showed that all constructs met the minimum threshold of reliability, with Cronbach's Alpha values ranging from 0.623 to 0.709. According to conventional standards, an alpha value of 0.7 and above is considered acceptable, although slightly lower values may still be deemed reliable in exploratory studies.

The construct for Credit Risk Management recorded a Cronbach's Alpha of 0.623, which, though marginally below the standard threshold, indicates a moderate level of internal consistency. This suggests that while the items measuring this variable are somewhat consistent, there is room for refinement in future studies to improve clarity and alignment. Cost of Debt attained a score of 0.706, which meets the recommended reliability level, indicating that the items within this construct were interpreted consistently by respondents and are therefore reliable for use in further analysis.

For Capital Structure, the alpha coefficient was 0.630, which, similar to credit risk management, reflects moderate reliability. While the score falls just short of 0.7, it remains acceptable for the purposes of this study and suggests that the construct captures the intended variable reasonably well. The Interest Rate construct yielded a Cronbach's Alpha of 0.692, which is slightly below the ideal but still demonstrates an adequate level of consistency. This means that the scale items were fairly cohesive in measuring interest rate volatility as it relates to financial performance.

Finally, the construct for Financial Performance achieved the highest reliability score of 0.709, surpassing the minimum benchmark. This indicates that the items used to measure financial performance were highly consistent and that the responses were aligned, providing confidence in the reliability of this section of the instrument.

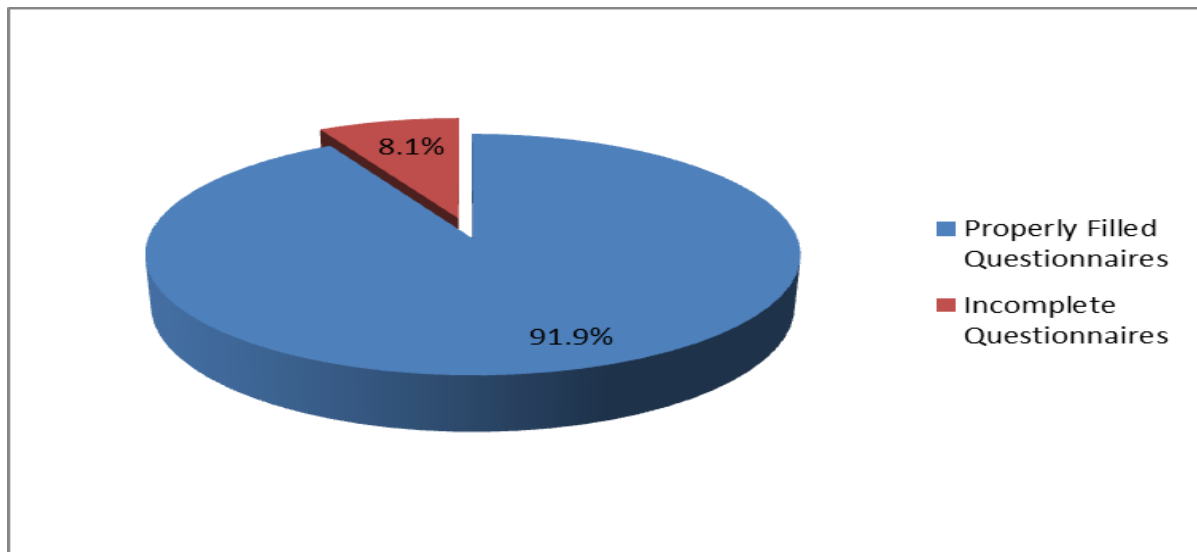
4.1.2 Analysis of Rate of Response

Table 5: Analysis of Rate of Response

Category	Frequency	Percentage (%)
Sample Size	148	100.0
Questionnaires Returned	140	94.6
Properly Filled Questionnaires	136	91.9

Source; Researcher (2025)

Figure 2: Analysis of Rate of Response



Source; Researcher (2025)

In research, the percentage of participants that successfully return completed questionnaires out of the intended sample size is known as the response rate. The researcher distributed 148 questionnaires to NCBA Bank workers for this study; 140 of them were returned, yielding a 94.6% response rate. A valid response rate of 91.9% was obtained from the 136 completed questionnaires that were judged to be correctly completed and suitable for analysis.

This high response rate shows how well the data gathering strategy worked, especially the drop-and-pick method that gave respondents enough time to finish the questionnaires. The favourable result was also probably influenced by the high degree of collaboration from NCBA Bank staff. Since it reduces the possibility of non-response bias and increases the generalizability of the study findings, Fincham (2008) states that a response rate of more than 80% is regarded as excellent in survey-based research.

Furthermore, the 91.9% rate of properly completed questionnaires indicates that the instrument was well-structured and clearly understood by participants, a critical factor in ensuring data quality. This is particularly important in quantitative studies where the reliability and accuracy of statistical analysis depend on the completeness and clarity of the data collected. As Babbie (2020) asserts, a high-quality response rate is not only a mark of effective survey administration but also a key element in ensuring the credibility and validity of research outcomes.

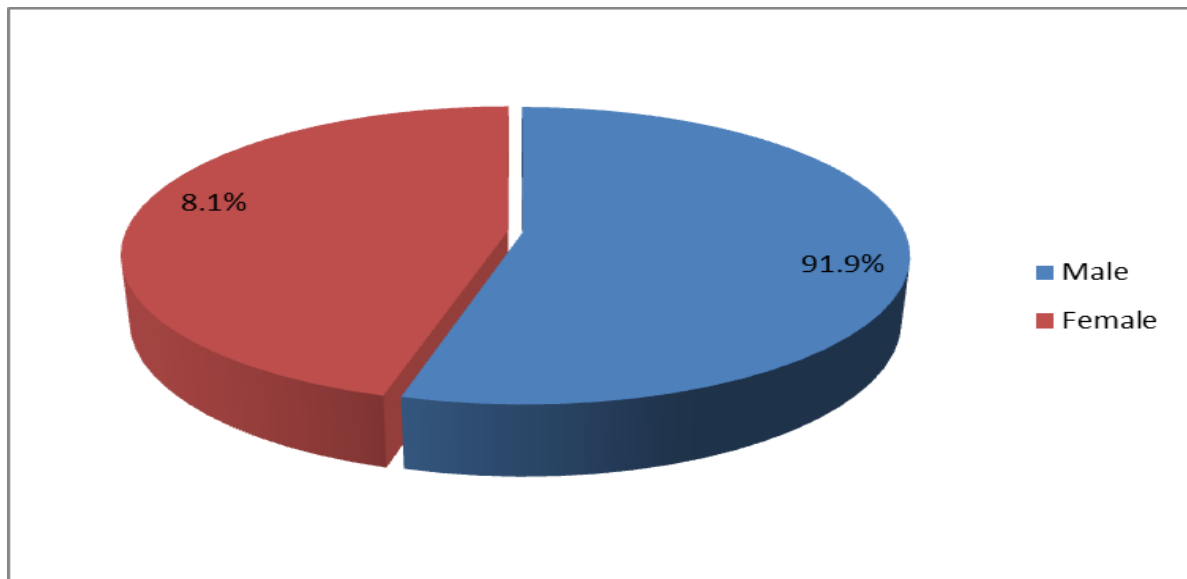
4.1.3 Gender Analysis

Table 6: Gender Analysis

Category	Frequency	Percentage
Male	74	54.4
Female	62	45.6
Total	136	100.0

Source; Researcher (2025)

Figure 3: Analysis of the Respondents Gender



Source; Researcher (2025)

The gender distribution of the respondents as revealed in the research showed that 62 (45.6%) were female and 74 (54.4%) of the 136 respondents that correctly completed the questionnaires were male. This implies that the NCBA Bank sample contained a slightly higher proportion of male employees than female employees.

The study's findings are more credible and inclusive because of the almost balanced distribution, which indicates that both genders were properly represented. Male respondents predominate by a little percentage, although this difference is not substantial enough to distort the study's findings. The increasing gender diversity in the banking industry, where both men and women play important roles in financial operations, risk management, and decision-making, is reflected in this composition.

From a research perspective, this gender representation is important because it ensures that the data reflects the views and experiences of both male and female employees, contributing to more comprehensive and unbiased findings. It also aligns with the principles of equitable representation in organizational studies, as recommended by Mugenda & Mugenda (2012), who emphasized the need for balanced demographic representation to enhance the generalizability and accuracy of survey-based research.

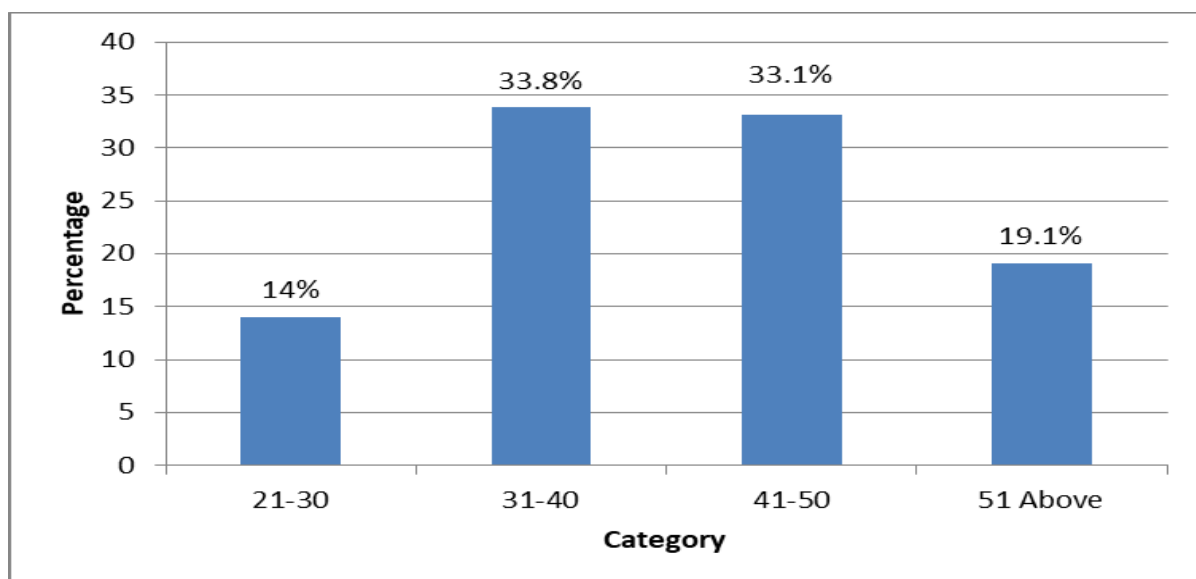
4.1.4 Age Distribution

Table 7: Age Distribution

Category	Frequency	Percentage
21-30	19	14.0
31-40	46	33.8
41-50	45	33.1
51 Above	26	19.1
Total	136	100.0

Source; Researcher (2025)

Figure 4: Respondents Age Distribution



Source; Researcher (2025)

The analysis of respondents' age distribution, based on the completed and valid questionnaires (n = 136), provides valuable insights into the demographic composition of employees at NCBA Bank. The findings show that the largest age group was those between 31 and 40 years, accounting for 33.8% (46 respondents). This was closely followed by respondents aged 41 to 50 years, who represented 33.1% (45 respondents). These two age brackets made up a combined 66.9%, indicating that the majority of employees fall within

mid-career age ranges, which typically include individuals with substantial professional experience and responsibilities within the organization.

Respondents aged 51 years and above comprised 19.1%, reflecting a significant presence of senior staff who likely hold leadership, supervisory, or specialized technical roles. This group brings institutional memory and strategic insight, especially critical in decision-making and mentoring roles within the bank. Meanwhile, youngest age group, 21 to 30 years, accounted for 14.0%, suggesting a moderate level of younger professionals at entry or early-career stages. Their presence points to active recruitment and growth opportunities for fresh talent within the bank. The age distribution indicates a healthy mix of experience, energy and innovation in workforce, which benefits for firm sustainability. According to Kothari (2004), such demographic diversity is vital for knowledge sharing, continuity and adaptability, particularly in banking where intergenerational collaboration enhances productivity.

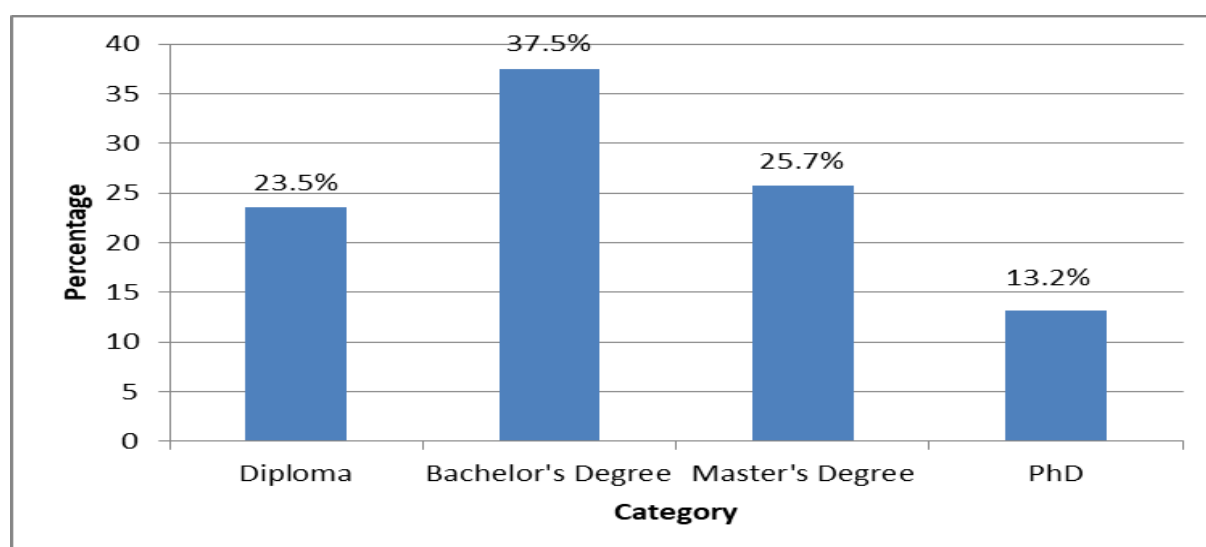
4.1.5 Highest Level of Education

Table 8: Highest Level of Education

Category	Frequency	Percentage
Diploma	32	23.5
Bachelor's Degree	51	37.5
Master's Degree	35	25.7
PhD	18	13.2
Total	136	100.0

Source; Researcher (2025)

Figure 5: Highest Level of Education



Source; Researcher (2025)

Based on the 136 properly completed questionnaires, reveals a highly educated workforce at NCBA Bank. The majority of respondents, 37.5% (51 individuals), reported holding a Bachelor's degree, which aligns with the common academic qualification required for most professional and technical roles in the banking industry. This group likely forms the core operational and managerial workforce of the organization, involved in finance, customer service, credit analysis, and related functions.

Following closely are those with a Master's degree, accounting for 25.7% (35 respondents). This significant representation suggests that a considerable portion of the staff has pursued advanced studies, equipping them with specialized skills and deeper financial knowledge. Employees at this level are typically found in middle to senior management roles, where strategic decision-making, leadership, and policy implementation are key.

Respondents with a Diploma qualification represented 23.5% (32 individuals). This group likely comprises early-career employees or those in operational support roles, contributing to the day-to-day functioning of the bank. Their presence indicates that the bank values practical skills and hands-on experience, not just academic credentials.

Lastly, 13.2% (18 respondents) reported having attained a PhD. While this is a smaller proportion, it signifies the presence of highly specialized professionals or consultants within the organization, possibly in roles involving research, innovation, risk management, or policy development. Overall, the data indicates that NCBA Bank employs a well-educated workforce, which is crucial for maintaining high performance standards in the competitive banking sector.

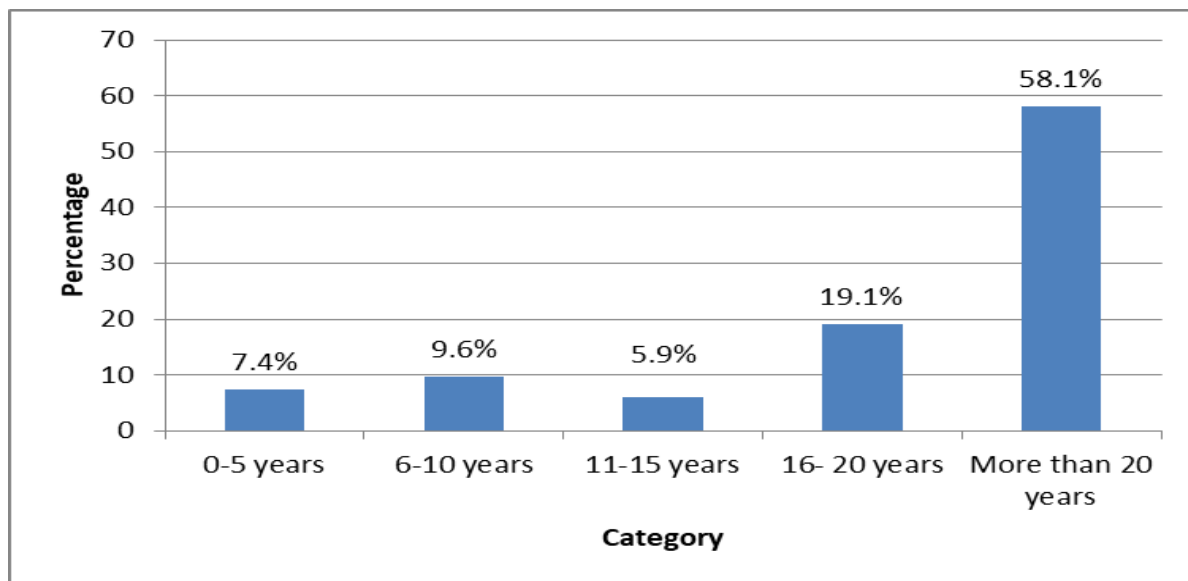
4.1.6 Respondents Years of Employment

Table 9: Respondents Years of Employment

Category	Frequency	Percentage
0-5 years	10	7.4
6-10 years	13	9.6
11-15 years	8	5.9
16- 20 years	26	19.1
More than 20 years	79	58.1
Total	136	100.0

Source; Researcher (2025)

Figure 6: Respondents Years of Employment in the Banking Sector



Source; Researcher (2025)

Important information about the degree of experience among NCBA Bank employees may be gleaned from the examination of respondents' years of banking industry employment. According to the 136 correctly filled-out surveys, 79 people, or 58.1% of the total, said they had more than 20 years of experience working in the banking sector. This is a strong indicator of a highly experienced workforce, which is crucial for institutional stability, knowledge transfer, and effective risk management in a complex and regulated industry like banking.

Another 19.1% (26 respondents) reported having worked between 16 and 20 years, reinforcing the observation that a large portion of the workforce has long-standing experience in the sector. These two categories combined represent 77.2% of the total respondents, suggesting that NCBA Bank is heavily staffed by seasoned professionals with deep industry understanding and long-term institutional loyalty.

The group with 6 to 10 years of experience made up 9.6% (13 respondents), while 7.4% (10 respondents) reported having 0 to 5 years of experience. Only 5.9% (8 individuals) fell into the 11 to 15 years bracket. The relatively small number of younger or less experienced employees may suggest a slower rate of recent recruitment or that junior staff form a smaller percentage of the sampled departments. However, it may also reflect a deliberate strategy by the bank to prioritize experienced professionals in key operational and leadership roles.

Overall, the data portrays NCBA Bank as an institution grounded in experience, which is advantageous in maintaining high standards of service delivery, compliance with regulatory frameworks, and effective financial decision-making. According to Mugenda and Mugenda (2003), employee experience enhances operational efficiency, especially in sectors that demand a high level of technical competence and customer trust, such as banking.

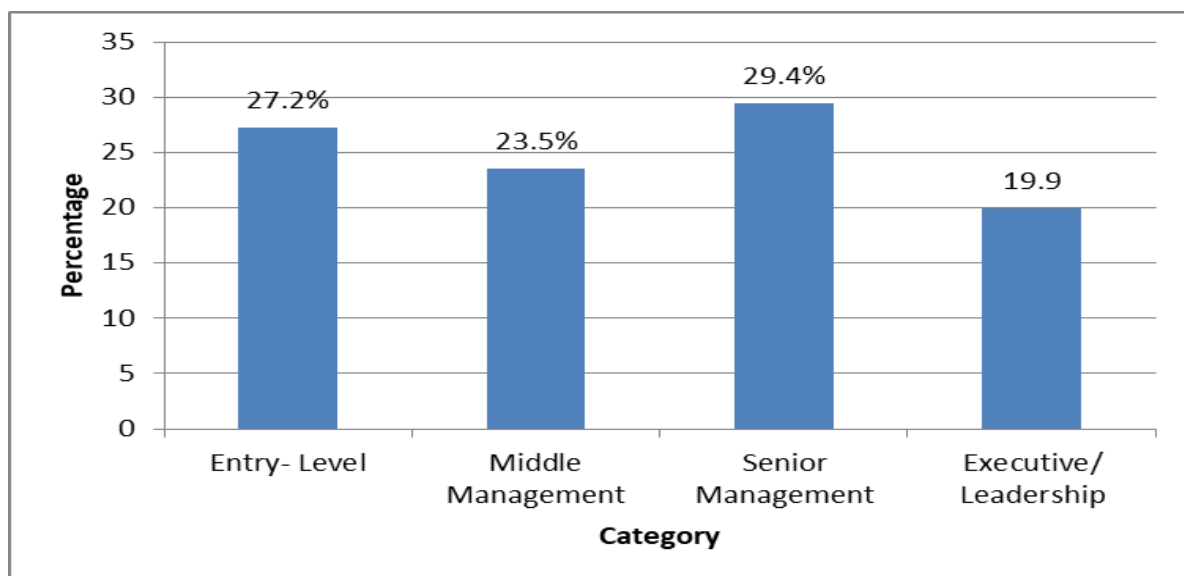
4.1.7 Respondents Job Position

Table 10: Respondents Job Position

Category	Frequency	Percentage
Entry- Level	37	27.2
Middle Management	32	23.5
Senior Management	40	29.4
Executive/ Leadership	27	19.9
Total	136	100.0

Source; Researcher (2025)

Figure 7: Respondents Job Position



Source; Researcher (2025)

The analysis of respondents' job positions provides a clearer picture of the organizational structure and representation of roles within NCBA Bank. Out of the 136 valid responses, the highest proportion of participants, 29.4%, identified as being in senior management. This suggests that the study successfully captured insights from a strategic leadership perspective, which is valuable when examining issues such as financial leverage, risk management, and long-term performance.

Entry-level staff accounted for 27.2% (37 respondents). Their inclusion provides a ground-level view of the bank's operations and helps in understanding how organizational strategies and financial policies are experienced at the implementation level. These staff members often interact directly with customers and are likely to provide practical insights into how financial practices translate into daily banking activities.

Middle management respondents made up 23.5% (32 individuals), representing a key link between strategy and operations. Middle managers play a crucial role in executing policies, managing teams, and translating executive directives into action. Their views are especially important when assessing the effectiveness and practicality of financial strategies and organizational systems.

Finally, 19.9% (27 respondents) were from the executive or leadership level, such as directors or heads of departments. These individuals are instrumental in decision-making and policy formulation. Their input contributes to a comprehensive understanding of the bank's financial strategy and risk appetite, especially regarding issues like capital structure and interest rate management. The diversity of job roles represented in the sample strengthens the reliability and depth of the study findings. It ensures that perspectives from across the organizational hierarchy are considered, allowing for a balanced assessment of how financial leverage practices impact performance across different levels of responsibility.

4.1.8 Descriptive analysis of Credit Risk Management

Table 11: Descriptive analysis of Credit Risk Management (N = 136)

Statements	Mean	Std. Deviation
The percentage of non-performing loans is a significant factor impacting the bank's financial performance.	4.02	1.352
The bank's financial performance is positively impacted by its loan payback rate.	4.36	1.059
The bank's capacity to turn a profit is impacted by the loan default rate.	4.21	1.123
The bank's financial results are significantly influenced by its exposure to credit risk.	4.34	1.097
Loan loss provision ratio is a crucial factor in managing the financial health of the bank.	4.10	1.284

The descriptive statistics on credit risk management at NCBA Bank provide crucial insight into how this factor influences financial performance. Based on the analysis of responses from 136 participants, the results show that credit risk management was generally rated positively across five key indicators, each with relatively high mean scores.

The statement “The bank’s financial performance is positively impacted by its loan payback rate” had the highest mean score of 4.36 (SD = 1.059), indicating strong agreement among respondents. This suggests that efficient loan recovery processes are viewed as a vital contributor to profitability and cash flow stability. This finding aligns with Poot (2020), who emphasized that institutions with structured credit collection frameworks often report better financial outcomes due to minimized revenue leakage.

The item “The bank’s financial results are significantly influenced by its exposure to credit risk” also received a high mean of 4.34 (SD = 1.097), showing broad consensus that managing credit risk exposure is critical to sustaining financial performance. Similarly, the loan default rate was noted to impact profitability, with a mean score of 4.21 (SD = 1.123), highlighting the negative implications of defaulted loans on earnings and capital adequacy.

Another critical aspect, the non-performing loans ratio, yielded a mean of 4.02 (SD = 1.352). Although slightly lower than the other indicators, it still reflects moderate agreement that high NPL levels threaten the financial health of the bank. This view is supported by Owusu-Antwi and Antwi (2020), who observed that rising NPLs erode investor confidence, reduce credit availability, and compromise liquidity factors that weaken financial resilience.

Finally, the loan loss provision ratio had a mean of 4.10 (SD = 1.284), reinforcing the perception that proactive provisioning for potential loan losses is a key strategy in safeguarding the bank’s balance sheet and maintaining regulatory compliance. These findings mirror the principles outlined by the Basel Committee on Banking Supervision (2025), which emphasizes provisioning and early risk recognition as central to sound credit risk practices.

The descriptive results are well supported by existing literature. For instance, Noja et al. (2021) argue that strong governance structures, including effective risk oversight boost both disclosure and financial outcomes. Their study of European financial service firms highlighted the importance of organizational practices that support robust credit risk frameworks.

Moreover, empirical findings by Njanike (2020) in the Zimbabwean banking context also revealed that effective credit risk control mechanisms such as monitoring systems, early warning tools, and compliance with loan policies, significantly improved the financial performance of commercial banks. These strategies reduce the incidence of bad debts and enhance operational efficiency

4.1.9 Descriptive Analysis of Cost of Debt

Table 12: Descriptive Analysis of Cost of Debt (N = 136)

Statements	Mean	Std. Deviation
One important measure of the bank's financial health is the interest expenditure to total debt ratio.	4.11	1.146
The average borrowing rate affects the overall profitability of the bank.	4.53	1.011
A higher debt-to-equity ratio has a detrimental effect on the bank's financial performance.	4.51	0.919
The bank's profitability and decision-making process are impacted by the Weighted Average Cost of Capital.	4.36	1.140
An essential indicator of the bank's capacity to meet its debt servicing commitments is the interest coverage ratio.	4.51	0.927

The descriptive statistics for cost of debt in this study offer a clear understanding of how debt servicing influences the financial performance of NCBA Bank. The analysis focused on five indicators, all of which received high average scores, indicating a strong consensus among respondents on the significance of managing the cost of debt.

The item “The average borrowing rate affects the overall profitability of the bank” had the highest mean score of 4.53 (SD = 1.011). This suggests that most respondents agree that borrowing costs directly affect profitability, as interest payments reduce net income. Closely related is the item “A higher debt-to-equity ratio has a detrimental effect on the bank’s financial performance,” which scored a mean of 4.51 (SD = 0.919). This response points to concerns about over-reliance on debt financing, which can burden the institution with unsustainable interest obligations, especially during economic downturns.

Additionally, the interest coverage ratio, which gauges the bank's capacity to pay interest, received a solid score of 4.51 (SD = 0.927), indicating that respondents saw this as a crucial sign of sound financial standing. A mean of 4.36 (SD = 1.140) was also obtained for the Weighted Average Cost of Capital, highlighting the need of maintaining a balance between debt and equity in order to maximize financing costs and profitability. Finally, the "Interest expenditure to total debt ratio" question had a score of 4.11 (SD = 1.146), indicating moderate to high agreement that this metric is essential for assessing how cost-effective the bank's borrowing practices are.

These findings align closely with earlier empirical studies. Murikwa (2017) observed that firms with high borrowing costs often experience weakened financial performance due to reduced liquidity and profitability. Similarly, Musiega et al. (2020) noted that when the cost of debt is efficiently managed, particularly through favourable interest terms and solid credit ratings, it results in increased returns on equity and improved overall financial performance. This is because reduced interest obligations free up resources for reinvestment, growth, and shareholder value creation.

Moreover, Chepkorir and Moronge (2020) highlighted that a high cost of debt exposes firms to financial distress and erodes investor confidence, especially in volatile markets. Their findings suggest that controlling debt expenses through strategic borrowing and financial planning enhances both short-term performance and long-term sustainability. The current study's findings reflect these insights, confirming that cost of debt is a critical determinant of bank profitability and financial health.

The descriptive analysis clearly indicates that employees at NCBA Bank recognize the central role of debt costs in shaping financial outcomes. Each of the five key indicators scored well above average, confirming that cost of debt is perceived as a strategic factor that must be carefully monitored and managed. These findings are in line with contemporary literature, reinforcing the idea that optimizing borrowing strategies and maintaining low-cost capital structures are vital to sustaining financial performance in the banking sector.

4.1.10 Descriptive Statistical Analysis of Capital Structure

Table 13: Descriptive Statistical Analysis of Capital Structure (N = 136)

Statements	Mean	Std. Deviation
The bank's debt-to-equity ratio is an important factor in determining its financial stability.	4.22	1.275
A higher level of capital adequacy guarantees the bank's resilience to financial shocks.	4.45	1.094
The profitability of the bank is directly impacted by the ratio of total debt to total assets.	3.94	1.315
The financial performance of the bank is negatively impacted by a high long-term debt ratio.	4.53	1.011
The ratio of retained earnings to total capital is crucial for enhancing the bank's financial performance.	4.51	0.919

The descriptive statistics from the study provide insightful information on how capital structure decisions are perceived by employees at NCBA Bank in relation to financial performance. The analysis was based on five key indicators, all of which showed relatively high mean scores, reflecting a strong awareness among respondents of the importance of capital structure in ensuring financial health and stability.

The statement “The financial performance of the bank is negatively impacted by a high long-term debt ratio” recorded the highest mean of 4.53 with a standard deviation of 1.011. This suggests that most respondents agree that an over-reliance on long-term debt weakens profitability, possibly due to the heavy burden of interest payments and reduced financial flexibility. This finding supports the concerns raised by Mwangi and Birundu (2020), who emphasized that high levels of long-term debt can increase a firm's vulnerability to interest rate volatility and credit constraints, ultimately harming financial performance.

Another highly rated indicator was “The ratio of retained earnings to total capital is crucial for enhancing the bank's financial performance,” which had a mean score of 4.51 (SD = 0.919). This reflects a clear understanding among staff of the value of internal financing in

reducing dependence on external debt and maintaining shareholder equity. The pecking order theory supports this view, advocating for retained earnings as the most cost-effective and least risky financing source for companies, particularly banks.

The statement “A higher level of capital adequacy guarantees the bank’s resilience to financial shocks” scored a strong mean of 4.45 (SD = 1.094), indicating that respondents recognize the protective role of adequate capitalization. Capital adequacy not only satisfies regulatory requirements but also acts as a financial cushion during downturns. According to Otieno and Nyang’au (2020), well-capitalized banks can absorb losses more efficiently, maintain operations, and preserve depositor confidence during periods of financial distress.

With a mean score of 4.22 (SD = 1.275) for the statement on the bank's debt-to-equity ratio as a measure of financial stability, it appears that everyone agrees that maintaining bank operations requires balanced leverage. According to the Trade-Off Theory, businesses should strive for the best possible capital mix to weigh the advantages of tax-deductible debt against the risks of possible financial trouble.

Lastly, the statement “The profitability of the bank is directly impacted by the ratio of total debt to total assets” had the lowest, but still relatively high, mean score of 3.94 (SD = 1.315). This implies a moderate perception that asset-heavy financing structures influence profitability, particularly when the cost of servicing debt outweighs the returns generated from asset deployment.

The findings of this descriptive analysis are well-supported by existing literature. According to Baker and Wurgler (2021), capital structure decisions significantly influence the value of a firm, with the optimal mix of debt and equity improving shareholder returns and financial performance. Similarly, Kumar and Singh (2024) note that while moderate debt levels offer tax advantages and enhance profitability, excessive debt introduces risks that may lead to financial instability and loss of investor confidence. Moreover, the study by Smith and Zhao (2024) emphasizes that financial digital transformation has also started shaping capital structure strategies, enabling banks to lower transaction costs and improve capital efficiency through better data-driven decision-making.

4.1.11 Descriptive Statistical Analysis of Interest Rate

Table 14: Descriptive Statistical Analysis of Interest Rate (N = 136)

Statements	Mean	Std. Deviation
Fluctuations in the Central Bank policy rate significantly affect the bank's financial performance.	4.36	1.140
Treasury bill rate movements influence the bank's profitability.	4.51	0.927
Variability in loan interest rates has an impact on the bank's revenue generation.	4.22	1.275
The bank's risk management and financial performance are impacted by changes in the inflation rate.	4.45	1.094
Changes in interbank lending rates have an effect on the bank's profitability and liquidity.	3.94	1.315

The Interest Rate variable's descriptive statistics shed light on the ways in which different interest rate components affect NCBA Bank's financial performance. All five of the study's items had high mean scores, indicating that respondents firmly believe that changes in interest rates have a significant influence on bank profitability and risk exposure.

The item with the highest mean score, "Treasury bill rate movements influence the bank's profitability," had a standard deviation of 0.927 and a mean score of 4.51. This indicates that respondents think government-issued short-term securities have a big impact on activities that generate income, especially for banks that invest in them. According to Karuiru and Muturi (2020), changes in treasury rates have a direct effect on banks' net returns and investment choices.

The second-highest rating was for the item "The bank's risk management and financial performance are impacted by changes in the inflation rate", which had a mean of 4.45 (SD = 1.094). Inflation erodes purchasing power and can lead to higher borrowing costs, influencing the bank's asset quality and income. This aligns with Otieno and Odhiambo (2020), who explained that inflation volatility affects banks' operating environments and interest margins, thus impacting overall financial performance.

Fluctuations in the Central Bank policy rate followed closely, with a mean of 4.36 (SD = 1.140), indicating strong agreement that monetary policy shifts, such as base rate changes,

significantly influence lending and deposit interest rates. Respondents recognize that changes in the Central Bank Rate (CBR) alter the cost of funds and determine credit availability—key drivers of bank earnings.

The item “Variability in loan interest rates has an impact on the bank’s revenue generation” received a mean score of 4.22 (SD = 1.275), reflecting an understanding that unpredictable lending rates can either enhance or suppress loan income. This is particularly important for banks with a significant portion of variable-rate loans, which are more sensitive to market movements.

The lowest-rated item was “Changes in interbank lending rates have an effect on the bank’s profitability and liquidity”, with a still-high mean of 3.94 (SD = 1.315). This suggests that while interbank rates are recognized as influential, they may be perceived as less impactful than government policy or inflation, possibly due to limited exposure or effective internal risk controls.

The results are in line with the literature assessment, which emphasizes how important interest rate volatility is to banking performance. Interest rate risk is one of the biggest financial hazards that banks, particularly those with sizable portfolios of interest-sensitive assets and liabilities, must deal with, according to the Basel Committee on Banking Supervision (2025).

Karuiru and Muturi (2020) found that rising interest rates increase the cost of borrowing and reduce consumer and business loan uptake, thereby weakening income streams. Furthermore, Otieno and Odhiambo (2020) argue that frequent interest rate fluctuations compress net interest margins and impair asset-liability matching, potentially resulting in lower profitability.

Empirical evidence from emerging economies also shows that unstable interest rates introduce planning uncertainty, discourage investment, and require sophisticated risk management strategies such as interest rate swaps or duration gap analysis to hedge against volatility

4.1.12 Descriptive Statistical Analysis of Financial Performance

Table 15: Descriptive Statistical Analysis of Financial Performance (N = 136)

Statements	Mean	Std. Deviation
An accurate indicator of a bank's financial health is its return on assets.	3.95	1.318
Return on Equity reflects the bank's overall financial performance and profitability.	3.86	1.394
The bank's profitability is mostly determined by its net interest margin.	3.84	1.431
One crucial measure of the bank's financial stability is the liquidity ratio.	3.80	1.465
The bank's profitability is mostly determined by its net interest margin.	3.84	1.431

The descriptive analysis of financial performance focused on five key indicators to assess how effectively NCBA Bank utilizes its financial resources. The data revealed moderate mean scores across all indicators, suggesting that while the bank's performance is viewed as stable, there is still room for improvement in operational efficiency and profitability metrics.

The answer that received the highest mean score, 3.95 with a standard deviation of 1.318, was "A bank's return on assets (ROA) is an accurate indicator of its financial health." This indicates that most respondents agreed that ROA is a good indicator of how well a bank uses its resources to produce revenue. Since ROA shows profitability in relation to the bank's total assets and is essential for internal decision-making and investor analysis, its significance in assessing financial performance is well accepted in the literature.

Following closely was "Return on Equity (ROE) reflects the bank's overall financial performance and profitability," with a mean score of 3.86 (SD = 1.394). This demonstrates recognition that ROE serves as a strong indicator of how well the bank uses shareholders' funds to generate profit. The findings align with the work of Darno and Gelatan (2025), who emphasized that strong ROE figures often reflect sound financial leverage practices and effective capital management strategies.

Two items tied for the next highest mean: “The bank’s profitability is mostly determined by its net interest margin (NIM),” both scoring 3.84 (SD = 1.431). These scores suggest that respondents view interest income as a significant driver of financial results, especially given the bank’s core lending and deposit functions. According to Karanja (2023) and the Kenya Bankers Association (2023), NIM is a key profitability metric for Kenyan commercial banks, often impacted by interest rate volatility and regulatory lending ceilings.

The item “One crucial measure of the bank’s financial stability is the liquidity ratio” scored the lowest, with a mean of 3.80 (SD = 1.465). While still within a moderate range, this indicates a slightly weaker perception among employees regarding liquidity as a primary performance indicator. This may reflect confidence in the bank’s liquidity management systems or a view that profitability indicators carry more weight in performance evaluation. Nevertheless, liquidity remains a vital factor in assessing a bank's short-term solvency and operational continuity, especially during market shocks.

The findings from this analysis are consistent with recent empirical studies emphasizing the multidimensional nature of financial performance in banking. Zhang and Qi (2023) found that digital transformation, through mobile, agency, and online banking improves asset utilization and boosts both ROA and ROE, particularly when paired with robust risk controls. Likewise, McKinsey & Company (2023) noted that banks that invest in artificial intelligence and big data analytics typically achieve higher profitability due to enhanced decision-making and cost reduction strategies. Additionally, the World Bank (2023) observed that strategic management, regulatory compliance, and innovation drive the resilience and performance of banks, particularly in emerging economies like Kenya. The findings of this study support these insights, showing that performance metrics such as ROA, ROE, and NIM are perceived as critical, though subject to macroeconomic and operational risks.

4.1.13 Linear Regression Analysis

Table 16: Model Summary of the Linear Regression Analysis between Financial Leverage and Financial Performance of NCBA Bank

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.384 ^a	0.148	0.122	4.86903

a. Predictors: (Constant), Interest Rate Value, Credit Risk Management, Cost of Debt, Capital Structure

The study's regression model research sheds crucial light on the relationship between NCBA Bank's financial performance and financial leverage factors, including interest rates, capital structure, cost of debt, and credit risk management. According to the model's R-value of 0.384 and R-squared (R^2) value of 0.148, the chosen independent variables account for around 14.8% of the variation in financial performance. Though additional variables not included in the model may potentially be important, the limited explanatory power indicates that these parameters have a quantifiable influence on financial performance. The model's somewhat diminished but still valid explanatory strength is confirmed by the modified R^2 of 0.122, which takes the number of predictors into consideration. The average difference between the actual and anticipated financial performance ratings was shown by the standard error of the estimate, which were 4.869.

4.1.14 ANOVA Analysis

Table 17: ANOVAa Analysis

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	538.141	4	134.535	5.675	.000b
	Residual	3105.676	131	23.707		
	Total	3643.816	135			

a Dependent Variable: Financial Performance

b Predictors: (Constant), Interest Rate Value, Credit Risk Management, Cost of Debt, Capital Structure

The model's overall significance was tested using ANOVA, which produced an F-statistic of 5.675 and a p-value of 0.000. This result indicates that the regression model is statistically significant and that the combination of credit risk management, cost of debt, capital structure, and interest rate meaningfully influences the bank's financial performance. The regression coefficients further revealed the direction and strength of each independent variable's relationship with financial performance.

4.1.15 Analysis of Coefficient Determinant of the Independent Variable

Table 18: Analysis of Coefficient Determinant of the Independent Variable

Coefficients^a		Unstandardized Coefficients		Standardized Coefficients	
Model		B	Std. Error	Beta	t
1	(Constant)	7.211	3.701		1.948
	Credit Risk Management	.355	.108	.275	3.300
	Cost of Debt	-.479	.230	-.303	-2.085
	Capital Structure	.018	.349	.013	.051
	Interest Rate Value	.688	.310	.513	2.216

a. Dependent Variable: Financial Performance

Better credit risk management, such as efficient loan recovery, fewer defaults, and proper provisioning, appears to boost profitability, according to the positive and statistically significant coefficient of credit risk management ($B = 0.355$, $p = 0.001$). This bolsters the conclusions of Poot (2020), who highlighted how structured credit controls improve bank financial results. Conversely, there was a statistically significant inverse link between debt costs and financial performance ($B = -0.479$, $p = 0.039$). In line with the findings of Darno and Gelatan (2025), who cautioned that excessive debt commitments can strain financial resources and degrade firm performance, this suggests that greater borrowing costs lower net income and impede profitability.

However, the capital structure variable had no discernible impact on financial performance ($B = 0.018$, $p = 0.959$), suggesting that the ratio of debt to equity may not directly or significantly affect profitability in the context of NCBA Bank. The pecking order and trade-off theories contend that choosing the best capital structure can increase company value, which is in opposition to this conclusion. Last but not least, the interest rate variable showed a positive and significant effect ($B = 0.688$, $p = 0.028$), indicating that changes in interest rates may have a favourable impact on financial performance through investment returns or interest margins. This is in line with Karuiru and Muturi (2020), who found that effective interest rate management, can be leveraged to strengthen income in commercial banks.

In conclusion, the model demonstrates that credit risk management, cost of debt, and interest rate significantly influence financial performance at NCBA Bank. While capital structure was not a statistically significant factor, the other variables validate the importance of sound financial leverage practices in achieving and sustaining profitability. These findings are supported by the Basel Committee on Banking Supervision (2025) and the Kenya Bankers Association (2023), both of which advocate for strategic financial management in navigating the evolving challenges of the banking sector.

4.2 Limitations of the Study

This study has limitations even though it offers valuable insights into how financial leverage factors, credit risk management, cost of debt, capital structure, and interest rate affect NCBA Bank's financial performance. First, the study was restricted to NCBA Bank, which might have an impact on how broadly the results can be applied to other banks or industries. Although NCBA Bank is a significant player in Kenya's banking sector, its organizational structure, financial strategy, and risk exposure may differ from those of smaller or newer financial institutions.

Second, self-reported information gathered via structured questionnaires was used in the study. This method is prone to response bias, where respondents may provide socially desirable answers or withhold negative information, particularly on sensitive topics like credit risk and cost management. Additionally, some variables such as capital structure may not have been fully understood by lower-level respondents, potentially affecting the accuracy of responses.

Another limitation lies in the model's explanatory power. The regression model accounted for only 14.8% of the variation in financial performance, suggesting that other important variables such as operational efficiency, technological adoption, macroeconomic factors, and regulatory compliance were not included in the analysis but may have substantial influence.

Finally, the study's cross-sectional design made it difficult to evaluate long-term causal relationships. Given that the data was gathered at a specific moment in time, the results reflect perceptions and financial realities as they existed during the study period (2025), but they do not account for seasonal variations or future economic shifts that may alter financial performance trends.

4.3 Chapter Summary

The results of the study, which were based on information gathered from 136 respondents at NCBA Bank, were presented in this chapter. The analysis covered demographic characteristics of the respondents and detailed descriptive statistics for the independent variables credit risk management, cost of debt, capital structure, and interest rate as well as the dependent variable, financial performance. The descriptive results revealed that respondents generally agreed on the significant role of all four financial leverage factors in shaping financial performance, with credit risk management and cost of debt being particularly influential.

The reliability test confirmed that all study variables had acceptable Cronbach's Alpha values, indicating consistency of the questionnaire items. The regression analysis further showed that credit risk management; cost of debt, and interest rate had a statistically significant relationship with financial performance, while capital structure did not show a significant effect. The model explained 14.8% of the variance in financial performance, suggesting the presence of other unmeasured factors that may influence financial outcomes.

The findings were then interpreted and tied to empirical literature, highlighting both consistencies and variances with past studies. The chapter concludes with a reflection on the study's limitations, recognizing the contextual boundaries within which the results should be interpreted.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

The chapter also presents conclusions addressing the research objectives and hypotheses, and offers practical recommendations for policymakers, bank managers, and other stakeholders. Finally, it suggests areas for future research that extend beyond the current study's scope, with the overall goal of interpreting the results and offering insights for both academic and practical application.

5.1 Summary of the Study

The summary is organized according to the study's specific objectives, providing a clear overview of how each variable influenced the financial performance of NCBA Bank. The findings highlight the major trends, relationships, and implications observed during the study, setting the foundation for the subsequent discussion, conclusions, and recommendations.

Credit risk management was found to have a statistically significant positive relationship with the financial performance of NCBA Bank. Respondents largely agreed that effective credit risk controls such as proper loan monitoring, strict credit policies, and prompt recovery processes contribute positively to profitability and financial stability. The regression analysis supported this, showing a significant positive beta coefficient, meaning that improvements in credit risk management practices lead to better financial outcomes. According to Poot (2020) and Njanike (2020), institutions with strong credit risk frameworks typically handle non-performing loans more effectively, which improves return on equity (ROE) and return on assets (ROA). These findings are consistent with their findings. Thus, the study comes to the conclusion that keeping commercial banks financially sound requires a proactive approach to credit risk management.

According to the data, financial performance is negatively impacted by the cost of debt in a statistically significant way. Respondents indicated that higher interest obligations, expensive borrowing terms, and debt servicing costs reduce the bank's net income and limit its ability to reinvest profits. Regression results confirmed this relationship, with a negative beta value and a p-value less than 0.05, indicating statistical significance. This supports the findings of Musiega et al. (2020) and Chepkorir and Moronge (2020), who noted that high debt costs erode profitability and increase financial vulnerability. Therefore, controlling debt costs

through favourable credit ratings and efficient financial planning is crucial for optimizing performance at NCBA Bank.

The results of the study showed that the impact of capital structure on financial performance was statistically negligible. Regression study revealed that capital structure did not significantly predict changes in the bank's financial performance, despite some respondents acknowledging the importance of having a well-balanced mix of debt and equity. This suggests that other variables, such as credit risk management and interest rates, play a more influential role. The results challenge traditional expectations from Trade-Off Theory but are consistent with studies by Otieno & Nyang'au (2020), who observed that overly high debt levels can negatively impact profitability, especially if not strategically managed. Hence, while capital structure remains important, its impact may be conditional on other internal and external factors.

Contrary to popular belief that fluctuating interest rates hurt bank earnings, it was discovered that interest rate volatility had a statistically significant positive impact on financial performance. Respondents agreed that interest rate changes particularly those linked to central bank policy and treasury instruments affect revenue streams, including loan pricing and investment returns. Regression analysis showed a significant positive relationship, suggesting that NCBA Bank effectively capitalizes on favourable rate shifts to enhance profitability. Karuiru and Muturi (2020), who pointed out that strategic interest rate management enables banks to sustain competitive margins, corroborate these findings. Thus, the study concludes that interest rate sensitivity, when properly managed, can be leveraged as an advantage rather than a threat.

5.2 Conclusion

This chapter has given a thorough overview of the research findings, connected them to the theoretical framework and examined literature, and offered useful suggestions based on the statistical analysis. The study's main goal was to find out how financial leverage affected NCBA Bank's financial performance by examining four important factors: interest rates, capital structure, cost of debt, and credit risk management.

As covered in Chapter Two, the Trade-Off Theory, Pecking Order Theory, and Agency Theory were among the important theories of capital structure and financial performance that served as the study's compass. These theories provided a conceptual foundation for examining how financial decisions particularly relating to debt and equity affect profitability

and operational efficiency. Businesses must weigh the advantages of debt (such tax shelters) with the risk of financial distress, as explained by the trade-off theory. According to the Pecking Order Theory, because of knowledge asymmetry, businesses favor internal funding first, followed by debt, and then equity. By imposing discipline, leverage can assist lower agency costs between managers and shareholders, according to the Agency Theory. Together, these views influenced how the study's results were interpreted and how the associations examined in the regression model were anticipated.

According to the regression results, the four independent variables account for 14.8% of the variation in financial performance, with an R-square value of 0.148. The statistical significance of the model ($F = 5.675$, $p = 0.000$) confirmed that the chosen financial leverage variables all have an impact on financial performance.

Financial performance was positively and significantly impacted by credit risk management on an individual basis ($\beta = 0.355$, $p = 0.001$). This complements empirical research that relates better asset quality and profitability to efficient credit control and validates theoretical expectations. In line with the Trade-Off Theory's prediction that excessive debt raises financial distress costs, ultimately impairing performance, the cost of debt demonstrated a negative and significant effect ($\beta = -0.479$, $p = 0.039$). However, capital structure was statistically negligible ($\beta = 0.018$, $p = 0.959$), indicating that the particular mix of debt and equity may not directly affect profitability in the context of NCBA Bank. Market conditions or institutionally specific financial strategies may be to blame for this surprising discovery. Finally, interest rates had a positive and substantial impact ($\beta = 0.688$, $p = 0.028$), suggesting that improving loan margins or investment yields by strategic positioning during interest rate swings boosts revenue.

In conclusion, the study validates the relevance of financial leverage variables particularly credit risk management, cost of debt, and interest rate as determinants of financial performance in the banking sector. The theoretical frameworks applied were instrumental in interpreting the dynamics observed, while the research methodology ensured accurate, reliable, and objective measurement of relationships. While capital structure was not a statistically significant predictor in this case, it remains conceptually important and may require further investigation across a broader sample or using a longitudinal design. The findings offer critical insights for NCBA Bank's management and the broader banking industry on strategic management of financial leverage to enhance institutional performance.

5.3 Recommendations

The NCBA Bank should prioritize continuous improvement of its credit risk assessment procedures. This includes enhancing due diligence during loan issuance, tightening credit scoring models, and investing in data analytics to detect early signs of default. Additionally, the bank should implement automated monitoring systems to ensure real-time tracking of loan repayment behaviour and enforce timely loan recovery measures. Strengthening staff training in credit appraisal and recovery processes can further mitigate default risk and maintain asset quality.

The study established that the cost of debt negatively impacts financial performance. To address this, the bank should engage in prudent borrowing by negotiating lower interest rates with lenders and maintaining a favourable credit rating. It is also advisable to diversify funding sources by leveraging more cost-effective financing options, such as long-term concessional loans or issuing corporate bonds at competitive rates. Effective debt planning and forecasting can also help align borrowing with periods of favourable market conditions, minimizing exposure to high-interest environments.

Although capital structure did not show a statistically significant effect in this study, it remains an essential component of financial planning. NCBA Bank should periodically assess its debt-to-equity ratio to ensure it maintains financial flexibility without over-relying on borrowed funds. Management should seek to strike a balance that supports business growth while minimizing the risks associated with financial distress.

The bank should continue to invest in robust asset-liability management systems to monitor interest rate risks and take advantage of favourable market trends. By maintaining an appropriate mix of fixed and variable rate instruments and using hedging tools like interest rate swaps, the bank can stabilize margins and protect earnings from rate shocks. Additionally, aligning loan and deposit pricing strategies with current central bank policies can improve competitiveness and profitability.

Across all dimensions, effective financial performance is tied to the bank's ability to monitor, report, and respond to emerging risks. NCBA Bank should establish an integrated financial risk dashboard that consolidates key indicators such as loan performance, debt cost trends, capital utilization, and interest rate exposure. This will empower management to make timely, data-driven decisions and enhance accountability at all levels. Regular audits and risk

reviews can further ensure compliance with both internal policies and external regulatory standards.

To support the implementation of these recommendations, the bank should continue to train its employees, particularly in departments involved in risk management, finance, and credit. Enhancing internal capacity in financial modelling, forecasting, and regulatory compliance will strengthen institutional resilience and drive performance. Additionally, educating customers on responsible borrowing and financial planning can improve loan repayment rates and reduce the burden of non-performing loans.

5.4 Implication of the Study

For those involved in the banking industry, the study's conclusions have a number of theoretical, practical, and policy ramifications, especially with regard to financial leverage and how it affects financial performance.

5.4.1. Managerial Implications

The results indicate that credit risk management, cost of debt, and interest rate significantly influence financial performance, with credit risk management having a positive effect while cost of debt had a negative one. This suggests that bank managers must place strong emphasis on strengthening internal credit appraisal systems, monitoring loan performance, and investing in risk management tools. At the same time, cost control in borrowing such as negotiating favourable loan terms or opting for more stable sources of funding can enhance profitability. By better managing these factors, NCBA Bank and other financial institutions can boost operational efficiency, minimize losses and safeguard stakeholder value.

5.4.2. Policy and Regulatory Implications

From a regulatory standpoint, the study provides useful insights for the Central Bank of Kenya (CBK) and other financial regulatory bodies. The finding that interest rate changes significantly affect financial performance implies that monetary policy decisions such as changes in the Central Bank Rate (CBR) have direct consequences for banking institutions. This calls for carefully balanced policies that stabilize inflation and borrowing rates without suppressing bank profitability. Regulators may also use these findings to encourage banks to maintain adequate capital buffers and develop stronger credit assessment frameworks to mitigate systemic risk.

5.4.3. Theoretical Implications

By evaluating the suitability of the Trade-Off Theory, Pecking Order Theory, and Agency Theory in the setting of a major Kenyan bank, the study adds to the body of knowledge. The usual theoretical expectation that leverage decisions directly affect firm value is challenged by the insignificance of capital structure non the regression model, even if the Trade-Off and Agency theories were particularly supported by the impact of credit risk and the cost of debt. This suggests a need to revisit or adapt these theories in light of sector-specific or regional dynamics, particularly in emerging markets like Kenya.

5.4.4. Academic and Research Implications

The study provides a valuable empirical foundation for scholars exploring the financial performance of commercial banks. The modest R^2 value of 0.148 shows that while financial leverage plays a role; other unexamined factors such as operational efficiency, technology use, customer satisfaction, or macroeconomic trends also influence performance. This opens new avenues for multi-variable or cross-country studies to expand the scope of financial performance research.

5.5 Future Research

Although this study offered important insights into the relationship between financial leverage and financial performance, it also revealed opportunities for further exploration.

First, the research was limited to a single institution NCBA Bank. Future studies should consider expanding the sample to multiple banks, including small, mid-sized, and Tier III financial institutions. This would allow for comparative analysis and better generalization of findings across the Kenyan banking sector.

Secondly, the R-square value of 14.8% implies that over 85% of the variation in financial performance remains unexplained by the selected variables. Future researchers should consider incorporating additional factors, such as operational efficiency, technological innovation, customer retention, macroeconomic indicators (like inflation and GDP), and regulatory compliance to gain a more holistic understanding of performance drivers.

Thirdly, this study adopted a cross-sectional design, which provides a snapshot in time but does not capture changes over time. Future research could adopt a longitudinal approach to assess how financial leverage decisions affect performance across different economic cycles or regulatory regimes.

Lastly, while this study relied on quantitative data, a mixed-methods approach that incorporates interviews or focus groups could provide richer insights into how financial managers perceive and navigate financial leverage decisions in practice. This could uncover underlying behavioural or strategic factors not captured through statistical analysis alone.

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Appendix I: Questionnaire

Bio data

1. Gender

Male []

Female []

Any Other Specify

2. Age Group (in complete years)

21-30 []

31-40 []

41-50 []

51 and above []

3. Highest Level of Education

Diploma []

Bachelor's Degree []

Master's Degree []

PhD []

Any Other Specify

4. Years of Employment in the Banking Sector

0-5 years []

6-10 years []

11-15 years []

16-20 years []

More than 20 years []

5. Position/Job Title

Entry-Level []

Middle Management []

Senior Management []

Executive/Leadership []

6. Duration of Employment in Current Department

Less than 1 year []

1-3 years []

4-6 years []

7 years and above []

SECTION 1: CREDIT RISK MANAGEMENT

1- Strongly Disagree, 2- Disagree, 3-Neutral, 4-Agree, 5-Strongly Agree

Statement	SD	D	N	A	SA
One important issue influencing the bank's financial success is the ratio of non-performing loans.					
The bank's financial performance is positively impacted by its loan payback rate.					
The bank's capacity to turn a profit is impacted by the loan default rate.					
The bank's financial results are significantly influenced by its exposure to credit risk.					
Loan loss provision ratio is a crucial factor in managing the financial health of the bank.					

SECTION 2: COST OF DEBT

1- Strongly Disagree, 2- Disagree, 3-Neutral, 4-Agree, 5-Strongly Agree

Question	SD	D	N	A	SA
One important measure of the bank's financial health is the interest expenditure to total debt ratio.					
The average borrowing rate affects the overall profitability of the bank.					
A higher debt-to-equity ratio has a detrimental effect on the bank's financial performance.					
The bank's profitability and decision-making process are impacted by the Weighted Average Cost of Capital.					
An essential indicator of the bank's capacity to meet its debt servicing commitments is the interest coverage ratio.					

SECTION 3: CAPITAL STRUCTURE

1- Strongly Disagree, 2- Disagree, 3-Neutral, 4-Agree, 5-Strongly Agree

Question	SD	D	N	A	SA
The bank's debt-to-equity ratio is an important factor in determining its financial stability.					
A higher level of capital adequacy guarantees the bank's resilience to financial shocks.					
The profitability of the bank is directly impacted by the ratio of total debt to total assets.					
The financial performance of the bank is negatively impacted by a high long-term debt ratio.					
The ratio of retained earnings to total capital is crucial for enhancing the bank's financial performance.					

SECTION 4: INTEREST RATE VOLATILITY

1- Strongly Disagree, 2- Disagree, 3-Neutral, 4-Agree, 5-Strongly Agree

Question	SD	D	N	A	SA
Fluctuations in the Central Bank policy rate significantly affect the bank's financial performance.					
Treasury bill rate movements influence the bank's profitability.					
Variability in loan interest rates has an impact on the bank's revenue generation.					
The bank's risk management and financial performance are impacted by changes in the inflation rate.					
Changes in interbank lending rates have an effect on the bank's profitability and liquidity.					

SECTION 5: FINANCIAL PERFORMANCE OF COMMERCIAL BANKS

1- Strongly Disagree, 2- Disagree, 3-Neutral, 4-Agree, 5-Strongly Agree

Question	SD	D	N	A	SA
An accurate indicator of a bank's financial health is its return on assets.					
Return on Equity reflects the bank's overall financial performance and profitability.					
The bank's profitability is mostly determined by its net interest margin.					
One crucial measure of the bank's financial stability is the liquidity ratio.					
The operational effectiveness of the bank is efficiently gauged by the cost-to-income ratio.					

Appendix II: Introductory Letter



Date: 16th June 2025

TO WHOM IT MAY CONCERN

MOHAMMED KASSIM MWAKAMPYA MML/27/00276/3/22

This letter serves to introduce the above named who is a (**Master of Management and Leadership**) student and is interested in carrying out research on **Financial Leverage of Commercial Banks and their Performance in Kenya: A Case Study of the NCBA Bank Nairobi**

Any assistance accorded to him in pursuit of this study will be greatly appreciated.

Yours Sincerely,



 Dr. Juster Nyaga
Dean, School of Management and Leadership

Appendix III: Research Permit

 Ministry of Education, Science, Technology and Innovation National Commission for Science, Technology and Innovation Ref No: 251766	 NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION Date of Issue: 30/June/2025
RESEARCH LICENSE	
	
This is to Certify that Mr. Mohamed Mwakampya Mwakampya of The Management University of Africa, has been licensed to conduct research as per the provision of the Science, Technology and Innovation Act, 2013 (Rev.2014) in Nairobi on the topic: Financial leverage of commercial banks and their performance in Kenya: A case study of the NCBA bank, Nairobi for the period ending : 30/June/2026.	
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Appendix IV: Plagiarism Report



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Top Sources

- 12% Internet sources
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