

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

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## DECLARATION

I declare that this Research Project is my original work and has never been submitted for a degree in any other university or college for examination/academic purposes.

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This Research Project has been submitted for examination with my approval as the University Supervisor.

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## **DEDICATION**

This project is dedicated to my Family members. My loving husband Richard Otieno Ojuaya for having encouraged me throughout the entire period. My late daughter Ashley Atieno with whom I would have loved to share my success with. My mother Teresia Raini and Father Hezekiah Ogetange for being the ones in whose footsteps I follow. My beautiful sisters Eva, Violet, Monicah and Susan for always being there to give me encouraging words.

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## **LIST OF ABBREVIATIONS**

<b>ANM</b>	Agent Network Managers
<b>ANMC</b>	Agent Network Management Companies
<b>ATM</b>	Automated Teller Machine
<b>CBK</b>	Central Bank of Kenya
<b>CRB</b>	Credit reference Bureau
<b>E-BANKING</b>	Electronic Banking
<b>FSD</b>	Financial sector Deepening
<b>GDP</b>	Gross Domestic Product
<b>ICT</b>	Information Communication Technology
<b>MBS</b>	Mobile Banking Services
<b>MDG</b>	Millennium Development Goals
<b>MFBs</b>	Micro Finance Banks
<b>NIM</b>	Net Interest Margin
<b>NPLs</b>	Non-Performing Loans
<b>PIN</b>	Personal Identification Number
<b>ROA</b>	Return on Asset
<b>ROE</b>	Return on Equity
<b>SPSS</b>	Statistical Package for Social Science

## **ABSTRACT**

The banking business environment has changed and innovative technology has remained a key strategy for the banking sector to remain competitive. The banking fraternity has really transformed its financial operations by providing convenient and accessible services through mobile banking and internet banking. To this end banks are fast developing branchless banking such as ATM, internet and mobile banking among others (Laukkanen & Pasanen, 2007). Agency banking is among the latest inventions that have improved the banking services by increasing accessibility and convenience to customers. Agency banking model requires commercial banks to rely on the existing infrastructure such as supermarkets, hotels and petrol stations to reach out to customers. Banking agents are usually equipped with a combination of point-of-sale (POS) card reader, mobile phone, barcode scanner to scan bills for bill payment transactions, Personal Identification Number (PIN) pads, and sometimes personal computers (PCs) that connect with the bank's server using a personal dial-up or other data connection. To drive decision making, ensure appropriate agent set up and channel support and permit subsequent performance evaluation against the original strategic intent (Sidiek, 2008). The objective of this study was mainly to evaluate the extent to which the agency model has contributed to the financial performance of the commercial banks in Kenya. Performance measures adopted was Return on Equity. In summary, the study reveals that agency banking has significant positive effect on the ROE of the Kenyan banks. From the statistical analysis it's revealed that there is a significance level between the agency banking variables and the rate of return on Assets. This implies that agency banking is continuously improving leading to significance increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation. The recommendations are that commercial banks should fully embrace agency banking through adoption of improved technology for information security volume of to make it more reliable to the customers. The government should support the program more often and reduce the high compliance costs, bureaucracy in registration and high cost of taxation.



# **CHAPTER ONE**

## **INTRODUCTION**

### **1.1 Background of the Study**

There are many aspects of the financial performance that can be analyzed. This study focuses on financial performance of commercial banks in Kenya. Aburime (2009) observed that profit is the essential prerequisite of a competitive banking institution. It is not only a result but also a necessity of for successful banking in a period of growing competition on financial markets; hence the basic aim of every bank is maximizing profits.

The Kenya Bureau of Statistic Report (2011) indicates that more than 7 million adult rural Kenyans are either under-banked or unbanked. This is partly because of the high cost of maintaining the bank branches and the low nature of business transactions in rural Kenya, a situation which makes opening of new branches in the rural areas less productive ventures. At yet another level mobile technology has substantially penetrated rural Kenya and is likely to be an upward trend in the near future. Banks and other financial institutions which have traditionally relied on physically established branches to provide banking services are now gearing towards the adoption of mobile banking services as a form of branchless banking. To this end banks are fast developing branchless banking such as ATM, internet and mobile banking among others (Laukkanen & Pasanen, 2007).

Technological advancement has not only affected the way of living but has had an effect on the way people do their banking. The last decade has seen an incredible upsurge in mobile penetration in the developing world. However of great interest is that while mobile phones offers several features including the possibility of mobile banking and financial services or they have been deprived of the same. Here in Kenya half of the population especially the rural people has no idea on mobile banking. However, the outreach of mobile banking sector has been found to vary across the country (Ivantury & Mas, 2008).

### **1.1.1 Agency Banking**

Eisenhardt (1989) describes the agency theory as a result of the explored risk sharing among individuals and groups during 1960-1970. The problem found was when two cooperating parties have different attitudes towards risk and have different objectives in mind. The agency problem starts when the agent seeks and the fact that it's costly and difficult for the principal to observe the agents work. Therefore it's assumed that the agent will act in his or her own interest rather than the principal's (Bender, 2011) there is also the issue of moral hazard which refers to lack of effort from the agent and does not do as agreed upon. It's also difficult for the Principal to ascertain skills of agent which he claims to have in order to carry out the task given.

In addition to reforms instituted in 2012 allowing microfinance banks to offer their services in marketing offices and self managed agencies, there were further amendments to both the Banking Act in 2013 that allows the subcontracting of agents. It allowed use Agent Network Managers (ANM) or Agent Network Management Companies (ANMC), also known as aggregators, in overseeing the day to day operations of agents in addition to providing strategic information to the respective financial institutions. Their main mandates include ensuring compliance, managing liquidity and training of agents respectively. This provision is meant to allow banks and microfinance banks to achieve scale in their respective agency networks while adhering to service quality standards. Furthermore, banks and microfinance banks will be able to enter into single contracts with ANM rather than multiple contracts with individual agents.

### **1.1.2 Financial Performance**

Performance is the outcome of all of the organization's operations and strategies (Paul, 2007). Measuring financial performance accurately is critical for accounting purposes and remains a central concern for most organizations. Performance measurement systems provide the foundation to develop strategic plans, assess an organization's completion of objectives, and remunerate managers (Kinyanjui, 2009). Although assessment of performance in the marketing literature is still very important, it is also complicated (Mills, 2003). While consensual measurement of performance promotes scholarly

investigations and can clarify managerial decisions, marketers have not been able to find clear, current and reliable measures of performance on which marketing merit could be judged.

The financial performance of banks has been of great interest to academic research since the Great Depression Intern the 1940's. In the last two decades studies have shown that commercial banks in Sub-Saharan Africa (SAA) are more profitable than the rest of the world with an average Return on Asset (ROA) of two percent (Flamini et al, .2009) the reasons being the huge gap between the banked and nun banked also the fact that the investment is in high risk area. The banks need to explore other services other than money transfer to improve their performance through agency banking which include: secure operating systems capable of carrying out real time transactions, generating an audit trail and protecting data confidentiality and integrity. A study carried out in New York by (Trout,1981),on the battle for your mind found out that an organization which is competing in fast changing markets with fast changing technology must make things happen, it must innovate. If it does not innovate it risks being overtaken by competitors. Sometimes a business underestimates the competitive challenges it faces. He concluded that the risk of this happening is high when competitors react to potential challenges in much the same way.

### **1.1.3 Effect of Agency Banking on Financial Performance**

Commercial banks are big beneficiaries of the rapid growth of agency outlets. They have helped cut costs on expansion and staffing but it is important that the banks have clear strategic rationale for each agent it sets up. To drive decision making, ensure appropriate agent set up and channel support and permit subsequent performance evaluation against the original strategic intent (Sidiiek, 2008). This initiative will enhance financial access for those people who are currently unbanked or under (CBK2011). An evaluation of the role of agency banking on the performance of commercial banks in Kenya concluded that infrastructure cost and security influence the financial performance of commercial banks attributable to financial performance of commercial banks to a very great extent.

Mwangi (2012) sought to establish the role of agency banking in the performance of commercial banks and established that cost effectiveness associated with agency banks positively influence banks financial performance. Emergence of agency banking has resulted in increased number of transaction volumes as the banks can now access a large number of clients. Extending branch networks is often too expensive, but the development of appropriate technologies can provide one answer

Deposit taking has increased among commercial banks since the emergence of agency banking

#### **1.1.4 Commercial Banks in Kenya**

As at 31<sup>st</sup> December 2013, the banking sector comprised of the central bank as the regulatory authority, 44 banking institutions (43 being commercial banks and 1 mortgage finance company-MFG) 7 representative offices of foreign banks ,9 microfinance banks(MFBs),2 credit reference bureaus. Out of the 44 banking institutions, 30 locally owned comprise 3 with public shareholding and 27 privately owned. The 9 MFBs, 2 CRBS and 101 forex bureaus are privately owned (CBK, 2013).The Kenyan banking sector registered an improvement in performance in 2013 notwithstanding the marginal economic growth. It registered a growth in net assets and customer deposits. The Central Bank continues to ease the monetary policy. This is contributed by the stability in the exchange rate and the need to facilitate uptake of private sector credit and to realign interest rates in the economy.

Number of banks conducting agency banking increased to 13 as at December 2013 from 10 commercial banks in 2012.The number of approved agents increased from 7,144 to 23,477 at the end of December 2013.this represents 44% increase in number of licenced agents ,albeit the concentration of 92% of the agents in 3 large banks.The number of transactions inceased by 40% from 29,937,112 transactions recorded in 2012 to 42,055,854 transactions in 2013 (CBK, 2013).

Adam (2010) did a comparison of banking sectors in East Africa and noted that by African standards, Kenya's banking sector has for many years been credited for its size and diversification. Unlike most other countries in the region, Kenya has a variety of financial institutions and markets- banks, insurance companies, stock and bond markets – that provide an array of financial products. Notwithstanding this relative advantage, Kenya's financial system has failed to provide adequate access to banking services for the bulk of the population. Whereas the larger proportion of savings comes from small depositors, lending is skewed in favor of large private and public enterprises in urban areas. Financial services are expensive, as evidenced by high interest rate spread and account fees. Commercial Banks and Mortgage Finance Institutions are licensed and regulated pursuant to the provisions of the Banking Act and the Regulations and Prudential Guidelines issued there under. They are the dominant players in the Kenyan Banking system and closer attention is paid to them while conducting off-site and on-site surveillance to ensure that they are in compliance with the laws and regulations (CBK, 2011).

## **1.2 Research Problem**

Agent banking has seen banking has brought about drastic changes in the banking sector. Agency banking transactions cost far less to process than transactions at an Automated Teller Machine or branch, banks can make a profit handling even small money transfers and payments(Booz,2003).The adoption of agency banking is mainly geared towards improving market share by attracting and retaining their customers ,improving their financial performance and creating a variety of services, to this day it's not clear whether adoption of agency banking has led to increase in market share and financial performance.

Kamau (2012) studied the relationship between agency banking and financial performance of banks in Kenya. Using regression analysis, the study gave a negative and weak correlation between number of agents, deposits and withdrawal transactions undertaken through agents and financial performance of banks as meseasured by Return on Equity.Waithanji (2012) stated that relationship between agency banking and financial

deepening could not be conclusively determined due to the low number of banks that have implemented it and impact may become clearer once all banks adopt agency banking. This study addressed the following research question: the effects of agency banking on financial performance of commercial banks in Kenya.

### **1.3 Objective of the Study**

Main objective was to investigate the effect of agency banking on financial performance of commercial banks in Kenya.

The specific objectives are

- i. What is the effect of agency banking transaction volumes on financial performance of commercial banks?
- ii. What is the effect of agency banking deposits on performance of commercial banks?
- iii. What is the effect of loan repayment through agents on financial performance of commercial banks?

### **1.4 Value of the Study**

The study will be important to the management of commercial banks because the information gathered will help in strengthening the effective and efficient running of agency banking. The commercial banks will be enlightened on importance of adopting agency banking as a measure of improving financial performance. To the agent owners they will be enlightened on benefits of being agents which will lead to growth and expansion of agent outlets leading better financial performance and business growth.

The general public will gain a clearer perceptual understanding that an agent of a bank is as good as the bank itself or even better due to the added benefits. The study will also be useful to other researchers and scholars by contributing a body of knowledge by adding to the existing literature. It will become a source of information on the banking industry.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

The literature review provides the theoretical rationale of the problem being studied as well as what research has already been done and how the findings relate to the problem at hand. It helps avoid unnecessary or intentional duplication of materials already covered. The literature will be reviewed from, working papers, journals, books, reports, periodicals and internet sources.

#### **2.2 Theoretical Review**

This section will look at three theories supporting agency banking; Agency theory, competitive advantage and Innovation Diffusion theory.

##### **2.2.1 Agency Theory**

Mitnick (1973) proposed the agency theory; he introduced the now common insight that institutions form around agency and evolve to deal with agency, in response to the essential imperfection of agency relationships. He applied regulation extensively and introduced the study of delegation as the creation of agents in governments. Ross (1976) introduced the study of agency in terms of problems of compensation and contracting; agency was seen as incentives problem. Jensen and Meckling(1976) originated the institutional theory of agency and were the first to make explicit applications of agency theory to social institutions.Both continued buliding on the work of Ross.The basic assumption of agency theory is that principales intrest may not align with the agents thus causing a conflict which need to be resolved.The owners are termed as principals and the managers as agents.The managers role is to represent the owner's intrests and be indepenedent of management.the separation of control from owners means that managers will manage all the process of the organisation on behalf of the owners.

The principals have to bear agency costs which are borne in trying to enforce the contractual obligations between them and the agents. They arise out of the inefficiencies of the principal- agent relationship. Agency costs can be reduced by providing appropriate incentives to align the interests of both agents and principals. Though agent banking is very new in Kenya there are a number of studies that have been done regarding the Effect of agency banking on financial performance of commercial banks. Bushs & Mathisen (2005) Agency banking is a concept that allows banks to engage third parties to offer products and services on their behalf. An agency bank is an organization/company that acts on behalf of another bank, it thus cannot accept deposits or extends loans in its own name; it acts as agent for the parent bank. It is a retail outlet contracted by a financial institution or a mobile network operator to process clients' transactions. Rather than a branch teller, it is the owner or an employee of the retail outlet who conducts the transaction and lets clients deposit, withdraw, and transfer funds, pay their bills, inquire about an account balance or receive government benefits or a direct deposit from their employer (Central Bank of Kenya (CBK), 2010). The convenience of access to banking services and the extended hours that the agencies work has been the most attractive features to the customer (as most agencies work between 8am up to 8pm). The rural population especially has heartily welcomed this idea since they have had to sometimes go through Vexing experiences to access banking services due to the poor road infrastructure and high costs (Kaane,2007).

### **2.2.2 Competitive Advantage Theory**

According to Porter (1980), developing a competitive strategy is developing abroad formula on how business is going to compete, what its goal should be and what policies would be needed to carry out these goals. He observed a competitive strategy as a combination of the ends (goals) for which the firm is striving and the means (policies) by which it's seeking to get there.

Competitive advantage to a great extent is determined by how a company positions itself in the industry. Competitive strategy is concerned with how a company can gain advantage through a distinctive way of competing. It aims at establishing a profitable and



sustainable position against the forces that determine industry competition. According to Porter (1980), developing a competitive strategy is developing a formula on how business is going to compete, what its goal should be and what policies would be needed to carry out these goals. He observed a competitive strategy as a combination of the ends (goals) for which the firm is striving and the means (policies) by which it's seeking to get there.

Competitive advantages give a company an edge over its rivals and an ability to generate greater value for the firm and its shareholders. The more sustainable the competitive advantage, the more difficult it is for competitors to neutralize the advantage. Business positioning is a term used in business marketing to refer to the process by which marketers try to create an image or identity in the minds of their target market for its product, brand, or organization. This was first introduced by Trout(1969), in his magazine "Industrial marketing" and then popularized by Ries and Trout in their book "Positioning - The Battle for Your Mind." (Trout, 1981) Organizations therefore strive to gain competitive advantage which positions them better within the business environment. Understanding sources of sustained competitive advantage has become a major area of concern in the contemporary strategic management (McGahan A,1997) (Barney,1991) (Peteraf, 1993) (Flint G,2005).

In addition Barney (1991), emphasizes that competitive advantage is the basis for superior performance. Understanding the components of competitive advantage is therefore paramount to the finance managers who are tasked with the responsibility of ensuring long term survival and success of the firm. He advances an integrative framework called SELECT to help managers systematically examine the facets of management. These are substance, expression, locale effect, cause and time-span. Analyzing the advantage enables the firm to fully maximize on its potential and sustainability.

One of the views of financial management, resource-based view, stipulates that in financial management the fundamental sources and drivers to firms' competitive advantage and superior performance are mainly associated with the attributes of their resources and capabilities which are valuable and costly-to-copy. Building on the assumptions that strategic resources are heterogeneously distributed across firms and that these differences are stable overtime. Barney (1991) examines the link between firm resources and sustained competitive advantage. Four empirical indicators of the potential of firm resources to generate sustained competitive advantage can be value, rareness, inimitability, and non-substitutability. Firm resources include all assets, capabilities, organizational processes, firm attributes, information, knowledge, etc. controlled by a firm that enable the firm to conceive and implement strategies that improve its efficiency and effectiveness. Superior financial performance reached through competitive advantage will ensure market leadership. In Addition, the studies provide an understanding that business strategy like agency banking will have a profound effect on generating competitive advantage.

### **2.2.3 Innovation diffusion Theory**

According to Dillon and Morris (1996): Rogers (1983 & 2003) innovation is any idea, object or practice that is perceived as new by members of the social system and defined the diffusion of innovation as the process by which the innovation is communicated through certain channels over time among members of social systems. Diffusion of innovation theory attempts to explain and describe the mechanisms of how new inventions in this case internet and mobile banking is adopted and becomes successful (Clarke, 2007) stated that not all innovations are adopted even if they are good it may take a long time for an innovation to be adopted. The study further stated that resistance to change may be a hindrance to diffusion of innovation although it might not stop the innovation it will slow it down.

The factors that influence diffusion of an innovation include: relative advantage (the extent to which a technology offers improvements over currently available tools), compatibility (its consistency with social practices and norms of its users), complexity

(its ease of learning), triability (the opportunity to try an innovation before committing to use it) and observability (the extent to which the technology's output and its gains are clear to see)

Moore and Benbasat (1991) built on the work of Roger (1983) Moore and Benbasat (1991) built on the work of Roger (1983). Three of the seven innovation characteristics are directly borrowed from Rogers: relative advantage, compatibility, and trialability. The fourth characteristic, ease of use is a close relative to Rogers' complexity. It is worth noting that both relative advantage and ease of use are subjective characteristics since they can be viewed differently depending on an individual's perceptions. Innovations such as agency banking have assisted the banks to position themselves in a way that they will maximize revenues and minimize costs thus ensuring sound financial performance.

### **2.3 Determinants of Financial Performance of Commercial Banks**

The major determinants of financial performance can be classified as bank specific (internal) factors and macroeconomic (external) factors (Al-Tamimi, 2010; Aburime, 2005). The bank specific factors are within the scope of the bank to manipulate them and that they differ from bank to bank. They include Capital Adequacy, Liquidity Management and asset quality. External factors are beyond scope of banks and they cannot manipulate them.

#### **2.3.1 Capital Adequacy**

Capital is the amount of funds available to support the banks business and act a buffer incase of adverse situation. Greater capital reduces chances of distress. Banks capital creates liquidity for the bank due to the fact that deposits are fragile and prone to bank runs. According to Dang (2011), the adequacy of capital is judged on basis of capital adequacy ratio (CAR). Capital adequacy ratio shows the internal strength of the bank to withstand losses during crisis.

The capital structure of banks is highly regulated because it plays a major role in reducing the number of bank failures and losses to depositors when a bank as highly leveraged firms are likely to take excessive risk in order to maximize shareholder value at the expense of finance providers (Kamau,2009). The key question is usually how much capital is enough. Regulators would like to have a higher minimum requirement to reduce cases of bank failures, whilst bankers in contrast argue that it is expensive and difficult to obtain additional equity and higher requirements restrict their competitiveness.

Koech (1995) argues that high capital leads to low profits since banks with a high capital ratio are risk averse, they ignore potential ( risky) investments opportunities and as a result, investors demand a lower return on their capital in exchange for lower risk. Although capital is expensive, highly capitalized banks face lower risks of bankruptcy, lower need for external funding especially in emerging economies where external borrowing is difficult. Well capitalized banks therefore should be more profitable than lowly capitalized banks.

### **2.3.2 Liquidity Management**

This refers to the ability of the bank to fulfill its obligations, mainly of depositors. According to Dang (2011) adequate level of liquidity is positively related with bank profitability. The most common financial ratios that reflect the liquidity position of a bank according to the above author are customer deposit to total asset and total loan to customer deposits. When banks hold high liquidity, they do so at the opportunity cost of some investment which could generate high returns (Kamau,2009).

The trade off that generally exist between return and liquidity risk are demonstrated by observing that shift from term securities to long term securities or loans raises a bank's return but also increases its liquidity risks and inverse in is true. Thus a high liquidity ratio indicates a less risky and less profitable bank. Management is faced with the dilemma of liquidity and profitability. Although more liquid assets increase the ability to raise cash on short notice, they also reduce management's ability to commit credibly to

an investment strategy that protects investors which can lead to a reduction of the firms capacity to raise external finance.

According to CBK Bank Supervision Annual Report (2009), the average liquidity ratio for banking sector was 30.8% in 2009, 37.0% in 2008 which is way above the minimum liquidity requirement of 20%. CBK attributes this to the banking industry's preference to invest in less risky government securities. This could also be due to the restrictions placed on commercial banks at the discount window, coupled with thin interbank market, a high reserve requirement and preference of government securities.

### **2.3.3 Asset Quality**

Banks asset include current asset, credit portfolio, fixed asset and other investments. Loan is the greatest asset that generates income. Quality of loan portfolio determines the profitability of the bank. It has a direct bearing on the banks profitability. The highest risk facing a bank is the losses derived from delinquent loans. (Dang, 2011). A low ratio of nonperforming loans to total loans shows that the bank is performing well. Poor asset quality is one of the major causes of bank failures. It led to a lot of bank failures in Kenya in the early 1980s. During that period 37 banks collapsed following the banking crises (Mwega, 2009). Most of the banks Failed due to Non-Performing Loans (NPLs) and that most of the larger banking failures involved insider lending. CBK measures asset quality by the ratio of loan non performing loans to gross loans.

Kosmidou (2008) applied a linear regression model on Greece 23 commercial banks 1990 to 2002 using ROA and the ratio of loan loss reserve to gross loans to proxy profitability and respectively. The results showed a negative significant impact of asset quality to bank profitability. This was in line with the theory that increased exposure to credit risk is normally associated with decreased firm profitability indicating that banks would improve profitability by improving screening and monitoring of credit risk.

#### **2.3.4 External/Macroeconomic Factors**

Gross Domestic Product, Inflation and Interest Rate are some of the macro economic factors that affect the performance of banks. For instance, the trend of GDP affects the demand for bank assets. Gross Domestic Product (GDP) is the market value of all officially recognized final well and services produced within a country in a given year, or over a given period of time. It's often used as an indicator of a country's material standard of living. During the declining GDP growth, the demand for credit falls which in turn negatively affects the profitability of banks. During boom the demand for credit is high compared to recession (Athanasoglou et al., 2005). During this period the bank's profitability goes up as interest earned on loans increases.

Inflation is measured as the rate of increase in general price level. Problem with inflation is it results in inefficiencies and inequities that result from inflation-induced changes in relative prices. Relative price changes affect supply-demand relationships for bank products. It affects the level of distribution of income, asset values, cash flows and debt. Central banks play a role in trying to control inflation. Inflation affects the overall amount of credit available for businesses. High inflation can decrease the real rate of return on assets. (John & Bruce, 2003).

Lower real rates of returns discourage saving but encourage borrowing. At this point new borrowers entering the market are likely to be of lesser quality and are more likely to default. Banks may react to the combined effects of lower real returns on their loans and the influx of riskier borrowers by rationing credit. Only when inflation rises above some critical level. At very low rates of inflation, inflation does not cause credit rationing. This implies that beneath some threshold, higher inflation might actually lead to increased real economic activity.

Interest rates represent the cost of borrowing capital for a given period of time. Price changes are anticipated in the world and these expectations are part of the process that determines interest rates (Gardner and Cooperman, 2005). Banks exist to inter-mediate the transactions between demanders and suppliers of money at a given consideration.

Earnings from these transactions form banks traditional income generating activities. Commercial banks need to come up with opportunities to take advantage of interest rates in order to improve on their financial performance. Profitability is partly due to the difference in interest rates charged on loans and what is paid to suppliers of funds i.e interest rates spread. If the interest charged on loans is higher than interest paid to lenders then the banks profit is high.

## **2.4 Empirical Review**

Many studies have been carried out to look at the effects of agency banking on financial performance of commercial banks. Theory and empirical evidence point to the critical role that improved access to finance has in promoting growth and reducing income inequality.

### **2.4.1 International Evidence**

Wright (2002) in Zimbabwe sought to establish the convenience of agency banking .The study found that the average daily deposit (Z\$10) is the same as the fare cost to the bank. She also considered time wasted at the bank or ATM plus the opportunity cost of lost business. Savings for the client in this case would surpass 100 percent if an agent were nearby to provide the service. (Mas & Seidek, 2008) indicated that only about one-quarter of households in developing countries have any forms of financial savings with formal banking institutions: 10 percent in Kenya, 20 percent in Macedonia, 25 percent in Mexico, 32 percent in Bangladesh. Yet access to financial services, whether in the form of savings, payments, credit, or insurance, is a fundamental tool for managing a family's well-being and productive capacity: to smooth expenditure when inflows are erratic (occasional work, seasonality of crops), to be able to build up purchasing power when expenditures are large and sporadic (school fees, buying seeds), or to protect against emergencies (natural disasters, death in the family).

Ivatury and Mas (2008) established that agency banking leads to cost minimization by reducing maintenance cost of banks fixed assets such as buildings and cost of service delivery. He describe a system whereby the agent has a contract with at least one bank

but may service customers of other banks with which it does not have a direct contract as long as the agent transactions for these other issuing banks are governed by the contract between the agent and its own acquiring bank and a separate agreement between the issuing bank and acquiring banks. In comparison to the other countries, a relatively large proportion of the Brazilian population is 'banked'(43%). This can partly be attributed to the fact that Brazil has the largest agent network in the world and is widely cited as a country where banking agents have been successfully used to expand financial access. An extra 13 million unbanked people have been reached (AFI,2011) and more than 160,000 retail outlets turned into correspondents since 1999. These agents can be found in all municipalities in Brazil. Most agents are commercial establishments, such as grocery stores, post offices, notaries and lottery outlets. More than 47,000 of these outlets are authorized to handle deposits and open accounts (CGAP, 2010).

A study by Bold (2011) in Brazil found that some countries restrict the location of agents which at times becomes an obstacle to financial inclusion. Initially due to concerns that agents could threaten bank branches, Brazilian regulatory originally restricted agents only to municipalities that did not have bank branches. Experience has shown that overly restrictive location requirements can complicate business case for viable agent-based banking and ultimately work against financial inclusion goals. Real time nature of most of the agent services has enabled remote supervision, thereby obviating one of the central arguments for location restrictions. These regulations often impose some form of fit and proper requirements, mandating a form of agent due diligence that requires financial institutions to verify that aspiring agents are reputable and have no criminal records and that they have the finances to sustain the agents. These regulations usually attract extra costs which hamper the growth of agency banking thus affecting financial performance of banks.

#### **2.4.2 Local Evidence**

In an evaluation of the role of agency banking in the performance of commercial banks in Kenya, Mwangi (2011) concluded that some of the effects of regulations on the performance of commercial banks in Kenya attributable to agency banking were



influenced by board of directors and executive management, accountability and quality control. The study concluded that infrastructure cost and security influence the financial performance of commercial banks attributable to agency banking to a great extent. The study recommended that Agency banking should be given more attention on security measures including risk based approach and that the banks should find better ways of screening their agents to ensure that the large cash transactions handling is effectively carried out on their behalf. It also recommended that banks should find other services other than money transfer only to improve their performance through agency banking which include: secure operating systems capable of carrying out real time transactions, generating audit trail and protecting data confidentiality and integrity.

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

Kamau (2012) studied the relationship between agency banking and financial performance of banks in Kenya. Through review of secondary data, the study found that agency banking outlets were 9,748 active agents in 2011 from 8,809 in 2010 facilitating a total volume of 8.7 million transactions valued at 43.6 billion. Using regression analysis, the study gave a negative and weak correlation between number of agents, deposits and withdrawal transactions undertaken through agents and financial performance of banks as

measured by Return on Equity This study therefore is aimed at assessing the contribution of agency banking on financial performance of commercial banks in Kenya.

Murugi (2013) looked at effects of agency banking on financial performance of banks in Kenya. Annual reports on individual banks' financial performance were used to extract financial performance indicators. CBK's annual report and supervisory reports was also used to establish the number of agents registered and the total transactional value conducted through the agents. The variables of interests were: the cash withdrawal and deposit transactions done through agents; number of active agents; return on assets (ROA) to measure profitability; cost to income ratio (to measure cost efficiency in using agency banks); and, staff cost to revenue ratio to measure the reduction of human resource cost due to agency banking. The data was collected for the three-year period: 2010 to 2012.

The findings indicated that out of all the banks that have rolled up the service, Equity bank, Co-operative bank and Kenya Commercial Bank show significant performance index. The findings further showed that yearly performance improved significantly. This implies that agency banking is continuously improving leading to significant increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation. The study revealed a positive strong effect between agency banking and financial performance. The study further recommends that commercial banks should fully embrace agency banking through adoption of improved technology for information security to make it more reliable to customers.

## **2.5 Summary of Literature Review**

Despite the growth of agency banking in Kenya, research into the field is still limited. Most studies carried out on the effect of agency banking on financial performance of banks were done when few banks' offered agency banking. This could lead to false reflection of the current state since more banks have adopted agency banking. Mwangi (2012) sought to establish the role of agency banking on the performance of commercial banks and established that cost effectiveness associated with agency banks positively

influence banks financial performance. Kamau (2012) undertook a study on the relationship between agency banking and financial performance of banks in Kenya and established a negative and weak correlation between the two.

However, these studies were conducted on very few banks that had implemented agency banking and as such the findings might be outdated and false reflection of the current state since more banks have adopted agency banking. The relationship could not be conclusive due to few banks have implemented agency banking and the impact may be felt once more banks adopt it. To date a total of 13 banks have taken up agency banking (CBK 2013). It is against this background the study arises to fill the knowledge gap by studying the effect of agency banking on financial performance of commercial banks in Kenya.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

This section gives a detailed outline of how the study took place, how data was collected and analyzed .It outlines the research methodology, research design, population of study and data collection and analysis techniques.

#### **3.2 Research Design**

This study adopted a descriptive survey. Descriptive analysis helped the study to describe the relevant aspects of the phenomenon under consideration and provide detailed information about each relevant variable. The target of study was 13 Commercial banks offering agency banking (Appendix 11). Data was available from CBK's annual reports and bank supervisory reports. Descriptive design was the most appropriate as it enabled the study test the relationship between agency banking and financial performance of banks.

The study used regression analysis to find the relationship between agency banking in terms of number of agents and the volume of deposit, withdrawals, and loan repayment transactions undertaken through agents and the financial performance measured by return on equity. Regression was used to distinguish the relationship between parameters to be measured and the dependent variables using statistical package of social sciences (SPSS).

### **3.3 Population**

Population was the 13 banks licensed in Kenya to operate agency banking as at 31<sup>st</sup> December 2013. This was through a census study.

(Appendix 11)

### **3.4 Data Collection**

Data used was secondary data obtained from bank supervision reports. Data contained number of cash transactions (withdrawals and deposits) through agents, number of loan/utility payment and number of existing agents and number of accounts opened through agents. Also key is the percentage of bank transactions carried out through bank agents.

### **3.5 Data Analysis**

It used inferential statistics using statistical package for social sciences (SPSS). Data was analyzed by applying Pearson's correlation analysis and a multiple regression analysis. The use of multiple regression analysis was to investigate effect of two or more variables simultaneously. It established the relationship between agency banking and its effect on financial performance of selected commercial banks using various key performance indicators. Performance measure adopted was Return on Equity. ROE is an important measure and indicator of the bank's profitability since it gives an overall picture of how well the bank is doing.

### 3.5.1 Analytical Model

The analytical model to be used is as follows:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \epsilon$$

Where

Y=Financial performance measure given by Return on Equity.

Return on Equity is given by Net Income divided by Shareholders Equity.

$\alpha$  =Regression constant

$\beta_1$  to  $\beta_4$  =Regression coefficients

$X_1$ =Total number of Agents

$X_2$ =Volume of cash deposits done through bank agents divided by total cash deposits

$X_3$ = Volume of cash withdrawals transactions done through bank agents divided by total cash withdrawal transactions

$X_4$ =Volume of loans repayments via Agency banking divided by total loan repayment.

$X_5$ =Number of accounts opened through agency banking divided by total accounts opened

$X_6$ =Liquidity (Liquid assets/Short term liabilities)

$\epsilon$ = Regression model error term

To come up with the regression model, the dependent and independent variables were determined by type of data to be collected. The variables of interest were: the cash withdrawal and deposit transactions done through agents; number of accounts opened

through agents; number of active agents; number of loan repayment through agents and return on equity (ROE) to measure profitability.

### **3.5.2 Test of Significance**

Test for significance of regression in case of multiple linear regression analysis was carried out using the ANOVA. The test was used to check if a linear statistical relationship exists between the dependent variable and at least one of the predictor variables. Dependent variable was banks performance and predictors (constants) were volume of cash withdrawals, number of agents and volume of cash deposits via bank agents.

R is the correlation coefficient which shows the relationship between the study variables.

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable.

## **CHAPTER FOUR**

### **DATA ANALYSIS FINDINGS AND INTERPRETATIONS**

#### **4.1 Introduction**

In this chapter, the study provided two types of data analysis; namely descriptive analysis and inferential analysis. The descriptive analysis helps the study to describe the relevant aspects of the phenomena under consideration and provide detailed information about each relevant variable. For the inferential analysis, the study used the Pearson correlation, the panel data regression analysis and the t-test statistics.

#### **4.2 Findings**

From the findings Equity Bank registered highest (10,000) number of agents as per the year 2013, followed by Co-operative Bank, Kenya Commercial Bank and Post Bank as indicated by 6,000, 2,500 and 2,000 respectively. The findings further showed that yearly performance improved significantly from the year 2011 as shown by, 25% (2011), 36 % (2012) and 40% (2013) respectively. This implies that agency banking is continuously improving leading to significance increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation.



#### 4.2.1 Descriptive Statistics

**Table 4.1: Performance of Agency banking as per number of agents, number of transactions per agent and volume of money flowing through the agents as per 2013**

	Number of Agents	Number of Transactions per agent	Volume of money flowing through the agents	ROE	Mean	Std Deviation
Kenya Commercial Bank	2500	3450	9,500,000	56.04	3.671	0.6713
Equity bank	10,000	5600	75,800,000	60.04	2.013	0.5614
Co-operative Bank of Kenya	6,000	5100	40,240,000	41.0,	2.751	0.1251
Family Bank	120	516	2,014,800	25.5	1.504	0.051
Diamond Trust bank	150	3000	429,900	25.9	3.1211	0.9043
National Bank of Kenya	1500	5014	7,042,000	38.010	4.154	0.1525
First Community Bank	150	610	6,501,800	26.5	2.9150	0.38150
Post bank	2000	1389	2,600,000	22.2	3.599	0.678
Chase Bank (K) Ltd	600	825	1,200,650	35.6	2.5210	0.38162
NIC Bank Ltd	400	730	500,500	23.1	3.8218	0.98216
Citi Bank Ltd	200	1200	1,500,200	20.8	1.8285	0.5105
Consolidated Bank	200	215	586,680	30.6	2.0158	0.3925
Jamii Bora	300	681	1,670,800	40.6	1.9515	0.49125
<b>Total</b>	<b>16,050</b>	<b>25429</b>	<b>82,079,530</b>	<b>408.8</b>	<b>28.4852</b>	<b>4.38755</b>

*Source: Research Findings*

Further the study indicates that equity bank registered the highest number of transactions per agent, followed by co-operative bank and Kenya commercial bank as indicated by 5600, 5100 and 3450 respectively. This implies that banks have continuously performed significantly in agency banking leading to improved financial performance.

**Table 4.2: Evaluation of Commercial Banks Agency Banking 2011-2013 (Financial Performance)**

	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>Overall Index Evaluation</b>
Kenya Commercial Bank	3.39	3.46	4.34	4.01
Equity bank	4.45	4.60	4.72	4.84
Co-operative Bank of Kenya	3.31	3.98	4.38	4.48
Family Bank	3.23	3.36	4.14	3.15
Diamond Trust bank	2.81	2.45	3.34	3.56
National Bank of Kenya	2.58	2.468	3.09	3.44
First Community Bank	2.11	2.16	2.22	2.18
Post bank	2.02	3.32	3.20	2.637
Chase Bank (K) Ltd	1.82	2.01	3.152	2.061
NIC Bank Ltd	2.01	2.17	3.25	3.42
Jamii Bora	1.60	2.08	3.16	3.06
Consolidated Bank	2.50	2.95	3.01	3.65
Jamii Bora	3.05	3.65	3.82	3.01
Yearly Performance	25%	36%	40%	100%

***Source: Research Findings***

The Findings in Table 4.2 indicates that out of a total of 43 banks, 13 have rolled out the agency banking service with Equity bank, Co-operative bank and Kenya Commercial Bank showing significance performance index as shown by the overall evaluation of 4.84, 4.48 and 4.01 respectively.

### **4.3 Pearson's Correlation Coefficient Analysis for Agency Banking and Financial Performance**

In this section, the study measured the degree of association between the agency banking functions and financial performance i.e. if the agency banking services (number of agents, number of transactions per agent and volume of money flowing through the agents) will increase financial performance of commercial banks. From the a priori stated

in the previous chapter, a positive relationship is expected between the measures of agency banking and financial performance. Table 4.3 and 4.4 presents the correlation coefficients for all the services considered in this study.

**Table 4.3: Pearson's Correlation Coefficients Matrix for the Model (Financial Performance)**

		<b>Number of Agents</b>	<b>Number of Transactions per Agent</b>	<b>Volume of Money Flowing through the Agents</b>	<b>Financial Performance</b>
Number of Agents	Pearson Correlation	1	-.650(**)	-.452(**)	.536(**)
	Sig. (2-tailed)		.000	.000	.000
Number of Transactions per Agent	Pearson Correlation	.658(**)	1	.612(**)	.600(**)
	Sig. (2-tailed)	.000		.001	.000
Volume of money flowing through the agents	Pearson Correlation	.490(**)	.41 (**)	1	.529
	Sig. (2-tailed)	.000	.001		.076
Financial performance	Pearson Correlation	.542(**)	.600(**)	.629	1
	Sig. (2-tailed)	.000	.000	.080	

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

***Source: Research Findings***

From the correlation result for model, volume of money flowing through the agents has a strong positive correlation of 0.629 followed by the number of transaction per agent of 0.600. Number of agent was found to be positively correlated with financial performance (0.542) with financial performance which is significant at 1% and 5%. This implies that volume of money flowing through the agents have a positive effect on the level of financial performance in Kenyan banks due to increased profitability. Number of agents

and the number of the transactions per agent also showed significant contribution to financial performance. The outcome from the statistics is consistent with earlier studies by Lipton and Lorsch (1992); Jensen (1993); Yermack (1996); Bennedsen et al (2006); Harris and Raviv (2005). They all argued that larger volume of transactions leads to improved financial performance.

**Table 4.4: Chi-Square Test: Two-Sample Assuming Equal Variances Banks rolled Up Agency Banking Service and Banks Not Rolled up Agency Banking Service**

	<b>agency service</b>	<b>banking</b>
Mean	0.0812	
Variance	0.0019	
Observations	13	
Hypothesized Mean Difference	0	
Df	7	
t Stat	2.051	
P(T<=t) one-tail	0.0045	
t Critical one-tail	1.6812	
P(T<=t) two-tail	0.0125	
t Critical two-tail	2.153	
Mean	0.0592	

***Source: Research Findings***

From the Chi-square results, the efficient rolled up agency banking banks recorded a mean of 0.0812. The variance for the agency banking is 0.0019 with t- calculated of 2.051 is seen greater than the t-tabulated of 2.6812

Further the study carried out the hypothesis testing between agency banking and financial performance. The study findings are as shown below.

**Table 4.5: Agency Banking Vs Financial Performance**

				Financial performance	
Agency Banking Transaction Practices	Pearson	0.952			
Correlation		0.001			
Sig. (2-tailed)		13			
N					

***Source: Research Findings***

A Pearson coefficient of 0.952 and p-value of 0.001 shows a strong, significant, positive relationship between agency banking and financial performance by the commercial banks rolled to agency banking in Kenya. Therefore, basing on these findings the study rejects the null hypothesis that there is no relationship between agency banking and financial performance and accepts the alternative hypothesis that there exists a relationship between agency banking and financial performance.

#### **4. 3.1 Regression Result**

**Table 4.6 Regression Result**

Model	R Square	Adjusted R Square	Std. Error of the Estimate
1	.589	.584	.02127

***Source: Research Findings***

The calculated R<sup>2</sup> is 58.9% implying that 58.9% of the variation in the financial performance is associated with the changes in the explanatory variables.

**Table 4.7 Regression result**

Variable	Coef.	Std. Err.	t	P>t	[95% Conf. Interval	Interval
X1	0.02	0.18	0.11	0.01	-0.35	0.39
X2	0.06	0.06	-1.16	0.06	-0.18	0.05
X3	0.04	0.09	0.45	0.06	-0.14	0.22
X4	4.03	2.54	-1.59	0.03	-9.34	1.27
X5	1.06	0.78	1.36	0.04	-0.57	2.70
X6	-0.14	0.07	-1.95	0.07	-0.30	0.01
Constant	1.30	5.92	-0.22	0.83	-13.69	11.08

*Source: Research Findings*

**Dependent variable:** Y

**Independent variable;** X<sub>1</sub>, X<sub>2</sub>, X<sub>3</sub>, X<sub>4</sub>, X<sub>5</sub>, X<sub>6</sub>

Table 4.5 above shows the regression result for the relationship between financial performance and the explanatory variables. All the explanatory variables are statistically significant at 5% level of significant in explaining financial performance.

The resultant model becomes:

$$Y = 1.30 + 0.02X_1 + 0.06X_2 + 0.04X_3 + 4.03X_4 + 1.06X_5 - 0.14X_6$$

A unit increase in number of agents leads to 1.30 units increase in the financial performance of the commercial banks. A unit increase in banks deposits done through banks agent leads to 0.02 units increase in the financial performance. A unit increase in cash withdrawals transactions will result to 4.03 units increase in financial performance of the commercial banks. A unit increase in the number of accounts opened through agency leads to 1.06 units increase in the financial performance of commercial banks. However, a unit increases in liquidity leads to 0.14 units decrease in financial performance. With all other explanatory variables held constant, commercial banks will realize financial performance of 1.30 units.

#### **4.4 Interpretation of the Findings**

In summary, the findings indicates that out of a total of 43 banks, 13 have rolled out the agency banking service with Equity Bank, Co-Operative Bank and Kenya Commercial Bank showing significance performance index. However other banks that have rolled up the service did not show much significance performance index. The findings further showed that yearly performance improved significantly from 2011 to 2013. This implies that agency banking is continuously improving leading to significance increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation.

From the correlation result for model, volume of money flowing through the agents has a strong negative correlation of with financial performance. This implies that volume of money flowing through the agents have a positive effect on the level of financial performance in Kenyan banks due to increased profitability. Number of agents and the number of the transactions per agent also showed significant contribution to financial performance.. This owes to the fact that high-transaction though with low-balance accounts are common among the poor which brings about economies of scale (Podpiera,2008). Commercial banks have branches that are not close to the customer, thus, the customer is less likely to use and transact. Commercial banks penetration in Kenya is very low and client interaction with the network is driven by mobile phone use and so controlled by telecom firms. Besides, other bank-based delivery channels such as branches have high costs inherent in these traditional banking methods. Thus, agency

banking is an apt model used in delivering services in remote place or areas where bank branches are not in existence (Soares and Melo Sobrinho, 2007).

The findings show that commercial banks that had rolled up agency banking were more effect based on the number of agent signed by the commercial bank. Commercial banks provide cash deposit and withdrawal, balance enquiry, collection of documents in relation to account opening, loan application, credit and debit card application, collection of debit and credit cards, cheque book request and collection for their customers through agency banking.



## **CHAPTER FIVE**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Introduction**

This chapter summarizes the study and makes conclusion based on the results. The implications from the findings and areas for further research are also presented. This section presents the findings from the study in comparison to what other scholars have said as noted under literature review.

#### **5.2 Summary**

The study aimed to establish the status of agency banking in the country and the financial performance of the banks that have rolled up the agency banking service. The findings indicates that out of a total of 43 banks, 13 have rolled out the agency banking service with Equity bank, Co-operative bank and Kenya commercial bank showing significance performance index. However other banks that have rolled up the service (Family Bank, NIC Bank, Diamond Trust bank, ECO bank and Post bank) did not show much significance performance index. The findings further showed that yearly performance improved significantly from 2011 to 2013.

This implies that agency banking is continuously improving leading to significance increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation. From the findings Equity bank registered the highest number of agents as per the year 2013, followed by Co-operative bank, Kenya commercial bank and family bank. Further the study indicates that equity bank registered the highest number of transactions per agent, followed by co-operative bank and Kenya

commercial bank respectively. This implies that banks have continuously performed significantly in agency banking leading to improved financial performance. From the correlation result for model, volume of money flowing through the agents has a strong negative correlation of with financial performance. This implies that volume of money flowing through the agents have a positive effect on the level of financial performance in Kenyan banks due to increased profitability. Number of agents and the number of the transactions per agent also showed significant contribution to financial performance. They all argued that larger volume of transactions leads to improved financial performance. From the t-test result, the efficient rolled up agency banking banks recorded a higher mean while the non-efficient banks recorded a slightly lower mean. However, the variance for the efficient banks and the no-efficient banks also varied significantly.

### **5.3 Conclusion**

From the findings above, it can be concluded that majority of the banks in the country have not embraced agency banking where out of the 43 licensed only 13 out of the licensed rolled up with the agency banking service. It can further be concluded from the findings that Equity Bank is the most performing commercial bank as far as agency banking is concerned followed by Cooperative Bank and Kenya Commercial Bank. Agency banking has positively and significantly influenced performance of commercial banks.

Banking agents enable commercial banks to divert existing customers from crowded branches providing a “complementary”, often more convenient channel. They use agents to reach an “additional” client segment or geography. Otherwise, reaching poor clients in rural areas is prohibitively expensive for banks since transaction numbers and volumes do

not cover the cost of a branch. Banking agents that piggy back on existing retail infrastructure – and lower set up and running cost - play a vital role in offering many low-income people access to a range of financial services. Also, low-income clients often feel more comfortable banking at their local store than walking into a marble branch which increases the commercial banks' revenue.

Agency banks also improves banks performance as it reduces huge savings on cost of construction of bank premises and leasing costs than when banks are using the Agency premises. It also cuts on human resource expenses. The banks do not have to employ new staff to manage the agency and the cost of training if any is to the bare minimum. It further, saves on equipment like furniture and computers. Additionally, the convenience of access to banking services and the extended hours that the banking agencies work is attractive features to the customer. This also helps increase banks' revenue will minimizing costs.

#### **5.4 Recommendation Policy and Procedure**

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

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

Based on the findings and conclusions presented above, the study recommends that banks should cushion their agents from certain costs such as insurance costs, cash in-transit or premise setup costs. This will enhance performance of banking agents. Besides, capacity of agents banking in providing services can be enhanced by banks ensuring that agents have enough float that can serve more client in order to mitigate clients disappointment and increase the number of customers. They can do this by advancing credit to their agents. In addition, banks should educate and regulate their agents to ensure uniformity in service delivery so as to enhance customer confidence in agents. The study recommends that customers should be enlightened on the operation of agency banking in order to enhance their confidentiality. Additionally, the study recommended that agent frequently trained on the operation process and policies to eradicate occurrence of error and mistake that are highly hindering penetration of agency banking.

### **5.5 Limitations of the Study**

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

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

## **5.6 Suggestions for Further Studies**

There is need for further research undertaken which may include studies on the factors affecting the financial performance of the agent banks; the role of the government or regulatory framework in supporting the adoption of agency banking and the impact of agency banking to the financial sector deepening or financial inclusion and other related studies. This would help establish effect of agency banking regulations on agents performance and answer the question: Does regulation (from banks and CBK) stifle agency banking or otherwise?

It is further suggested that further research should be done on the challenges facing implementation of agency banking. Studies can also be conducted on the effectiveness of agency banking on banking outreach/penetration in Kenya. It is also recommended that, as roadmap to agency banking development in Kenya, further studies can be done on customer perception of agency banking so as to determine what affect banking agents' performance from the demand side. Moreover, studies can be done on the economic impact of agency banking model performance in Kenya.

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## **APPENDICES**

### **Appendix I: Commercial Banks Registered In Kenya As At 30<sup>th</sup> December 2013**

- 1) Bank of Africa (K) Ltd.
- 2) Bank of India
- 3) Citibank N.A. Kenya
- 4) Bank of Baroda (K) Ltd.
- 5) Barclays Bank of Kenya Ltd.
- 6) Consolidated Bank of Kenya Ltd.
- 7) City Finance Bank Ltd.
- 8) Commercial Bank of Africa Ltd.
- 9) Co-operative Bank of Kenya Ltd.
- 10) Credit Bank Ltd.
- 11) Charterhouse Bank Ltd.
- 12) Chase Bank (K) Ltd.
- 13) Diamond Trust Bank Kenya Ltd.
- 14) Development Bank of Kenya Ltd.
- 15) Ecobank Ltd
- 16) First Community Bank
- 17) K-Rep Bank Ltd.
- 18) Standard Chartered Bank (K) Ltd.
- 19) Gulf Africa Bank (K) Ltd
- 20) Prime Bank Ltd.
- 21) Habib Bank A.G. Zurich
- 22) Habib Bank Ltd.
- 23) Kenya Commercial Bank Ltd.
- 24) National Bank of Kenya Ltd.
- 25) Jamii Bora Bank Ltd.
- 26) CFC Stanbic Bank Ltd.
- 27) African Banking Corporation Ltd.
- 28) Dubai Bank Kenya Ltd

- 29) Eco bank
  - 30) Equatorial Commercial Bank Ltd
  - 31) Equity Bank Ltd.
  - 32) Family Bank Ltd.
  - 33) Fidelity Commercial Bank Ltd.
  - 34) Fina Bank Ltd.
  - 35) Giro Commercial Bank Ltd.
  - 36) Guardian Bank Ltd.
  - 37) Imperial Bank Ltd.
  - 38) Middle East Bank (K) Ltd.
  - 39) NIC Bank Ltd.
  - 40) Oriental Commercial Bank Ltd.
  - 41) Paramount Universal Bank Ltd.
  - 42) UBA Kenya Bank Ltd.
  - 43) Trans-National Bank Ltd.
  - 44) Victoria Commercial Bank Ltd.
  - 45) Housing Finance Ltd (Mortgage financial Institution).
- SOURCE: Bank Supervision Report 2013.

**Appendix II: Commercial Banks Adopting Agency Banking In Kenya As At 30th  
December 2013**

- 1) Kenya Commercial Bank Ltd.
  - 2) Co-operative Bank of Kenya Ltd
  - 3) Chase Bank (K) Ltd.
  - 4) Diamond Trust Bank Kenya Ltd
  - 5) Equity Bank Ltd.
  - 6) Family Bank Ltd.
  - 7) NIC Bank Ltd
  - 8) Post Bank Ltd
  - 9) Citi Bank Ltd
  - 10) Consolidated Bank
  - 11) Jamii Bora
  - 12) National Bank of Kenya
  - 13) First Community Bank
- SOURCE: Bank Supervision Report 2013.