EFFECT OF LEVERAGE ON EARNINGS QUALITY AMONG COMMERCIAL BANKS IN KENYA

BY

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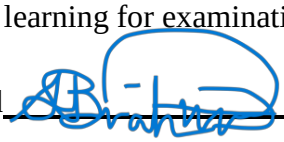
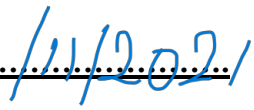
DECLARATION

I do hereby declare that this is my original work and has not been handed over to any institution of higher learning for examination.

Signed  **Date** 

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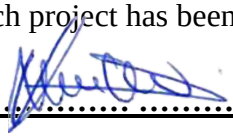
Supervisor

This research project has been prepared and submitted with our approval as the university supervisor.

Signed  **Date**24th November 2021

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DEDICATION

This Project is dedicated to my parents Madina Ali and Mohamud Ali who have been with me in every second of my life. They have been supporting me for my entire life.

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LIST OF ABBREVIATIONS AND ACRONYMS

ANOVA Analysis of Variance

CBK Central Bank of Kenya

KSE Karachi Stock of Exchange

NSE Nairobi Security Exchange

ROA Return on Assets

ROE Return on Equity

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ABSTRACT

Leverage and earning quality have been very paramount in the commercial banks. The fundamental aspect of commercial banks is the earning quality. It is crucial in the provision of relevant and accurate information to the investors. The banking sectors have undergone several milestones and evolved to reach the current state. Leverage and earning quality have been the pivotal areas. Earning quality has been the area of consideration for the investors in the current fast-paced commercial environment.

The research sought to investigate the effects of leverage on the earning quality of the commercial banks in Kenya. The research was anchored by the trade-off theory, pecking order theory and agency theory. Trade-off Theory stipulated the ability of the company to work sufficiently and adequately in optimizing debt-equity. Pecking order theory indicated that banks do not have one specific capital finance hence relies on the decision making. Agency theory anchored the principal-agent mandate assigned by the shareholders, and the need to maximize shareholder's wealth in the banking industry.

The determinants of the study included degree of financial leverage, banks size, management efficiency, and credit management. The study optimized descriptive research design for the 42 commercial banks in Kenya. The data sourced run for 5years spanning from 2016 to 2020. The analysis considered was linearity, normality, autocorrelation among others. The data was collected through secondary method and was taken through systematic steps before analysis. The research postulated that degree of financial leverage, management efficiency, and credit risk management had negative correlation with the earning quality. The bank size had positive association with the earning Quality.

CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

The transformations and unlocking of the opportunities in Kenya are paramount for growth. The achievement can be realized through operational excellence or profitability. Profitability promotes the financial well-being being of the company. Financial health enhances the ability of the company to undertake variety of activities. Furthermore, the companies have always unified capital while maximizing the shareholders wealth. The services must always be consolidated to guarantee drivers of developments (WorldBank, 2020). Financial health of the company is measured through profitability. Profitability establishes the financial leverage of the company. The company leverage deficiency possesses greater earning quality (Okumu, 2020).

The theories that reinforce this study by building a strong foundation. These theories are very important in the study since they expound on the research and provide insight information on leverage and earning quality management. Trade-off Theory states the ability of the firms to work adequately and appropriately by utilizing the debt-equity financial ratio. Pecking order theory states that the firm has no specific capital structure order, hence make decision based on their ability and corporate governance decisions. Agency theory indicates the assignment given to management by the shareholders. The shareholders mandate the management to promotes the ability of organization and structures while working towards maximization of shareholder's wealth.

Although earning quality has had significant emphasize on the financial accounting, the conceptualization has been overlooked. The nature and consequences of the earning management has not received the required attentions. Earning quality have associated with the adjustment of financial reports with the aim of reaching at desired goals. The fundamental aims of all these are earning management, earning smoothing, predictability, and conservatism (Dehow et al 2010). The study has received minimal considerations, yet the area is broad and multidimensional. The great diversity ranges from the reactions of the investors to earning quality to the utilization of asymmetric information.

1.1.1 Leverage

The companies struggling financial are motivated to manipulate the financial to shows the predictability and earning smoothening. The companies have utilized the different strategies in earning quality. Earning quality

is measurement tool showing abnormality in accruals, leverage, and struggling company. Earning smoothing is done to portray financial stability and predictable earning. The companies do earnings smoothing to conceal their leverage and financial distress. Financial leverage is the usage of borrowed funds to enhance business operation. It is used to broaden the asset-based investments (Babbie, 2017). The firms utilize principle of leverage to promote company's returns on Equity capital and majorly whenever the operating efficiency of the firm is growing their return on aggregate investment. Njeri (2015) described leverage as an amplifier that increases or decreases the earnings. John & Cheng (2018) indicated that leverage is utilization of borrowed funds to maximize the investments. Muthuri (2018) opined that leverage indicates the longevity strength financial health of a firm. In nutshell, leverage is risking the exposure to financial distress while focusing on the high profits and returns.

The results portray that company with leverage deficits can experience greater earning quality. Low-leveraged companies lower the earning quality while the highly-leverage firms have more earning quality hence prioritize the equity funding. Furthermore, the company prioritize to engage in the realistic earning management prior to external funding. Some companies prefer to undertake accrual-based method of earning management prior to choosing equity. The high-leveraged firm has more difficulty than low-leverage while undertaking real earning management (Yusuf, 2020). This is spearheaded before debt funding choice. The leverage is measured using the total debts as a percentage of total assets. This method of will be useful in this study.

1.1.2 Earning Quality

Earning quality provides information of relevance of earning as a parameter indicating firms performance. Earning quality considers the accounting principles. Furthermore, it focuses on the statement of financial position and income statement to measure earning Quality (Dehow, 2010). Earnings in the companies are based on projections, estimations and preposition of the accounting principles (Baik et al, 2019). Earning quality is very crucial in measuring the relevance of financial statements (Alhadab, 2015). Furthermore, it is critical factor considered in economic performance and how the financial statement can accurate projects the future financial outcomes of the firm.

Equality Quality determines the financial credibility of the company. It promotes the relevance and the sound application of financial principles. Earning Quality illustrates the futuristic position of the firm. Furthermore, it portrays the proportion of earnings to the operational activities. The continuous increase in revenue leads to increase in gross profit and net profit when all other factors are constant. The usefulness of earning quality is on the reliable and credible reports (Alhadab, 2015). The investors need the earning quality to predict the future of the firm. This is supreme in the valuation of the company futuristic position. The study is paramount in establishing the role of financial leverage on the earning quality.

Previous scholars have used different metrics in measuring earning quality. Lyimo (2014) postulated that EQ is measurable on accrual quality, persistence and predictability. Mano (2018) utilized the operating cash and profit to indicate the earning quality. The closer the ratio to one, the greater the earning quality. Yusuf (2020) stipulated the use of accrual quality and earning persistence while Teets (2012) indicated that earning quality is a reflection of the well-being of the financial state of the firm. It is very important in future prediction and valuation of the company. Earning quality will be measured using the accrual quality method.

1.1.3 Leverage and Earning Quality

Earning Quality is a futuristic indicator of financial performance. It provides full disclosure on the earnings. It is a crucial indicative of the future cashflows. Earning quality promotes the principles of accounting that reinforces the faithful representations, reliability, relevance, truthful and fair view information. Leverage advocates for the use of debts in the investments. Leverage is the precursor of earning quality. It is a forward-looking application of debts and equity to maximize the net present value. Earnings provides more elaborated information. Earning quality is financial projection tool that investors use in decision making on whether to or not to invest (Qamar et al., 2015).

Leverage and Earning Quality are very important to the investors and shareholders. Both of them are futuristic in nature. Earning quality reflect the aggressive usage of accounting methods, inflation, and disposal of assets for a gain. The investors use leverage and earning quality in estimating the future performance. Hassan & Farouk (2018) concluded that leverage posted a significant effect on the earning quality. The sensitivity of company returns (Leverage) is anticipated to have a positive correlation with earning quality. It affects the quality reporting through smoothing and earning management. Leverage is

sensitive to the manipulation of earning quality. Furthermore, reliability, credibility, faithful representation are very important in both leverage and earning quality. In a nutshell, leverage and earning quality are tied together.

1.1.4 Commercial Banks in Kenya

Commercial Banks in Kenya are mandated and work under regulation of CBK. The crucial jurisdiction of CBK is the licensing. It is stipulated through Companies Act (489), Banking Act Cap (488). Moreover, the regulation and control of banks is well illustrated under CBK cap (491) in cognizant of methodical risk mitigation strategies. CBK ensures that commercial banks follow the stipulated regulations.

The commercial banks have grown drastically with presence of 42 commercial banks. The commercial banks undertake several functions including deposit and advancing loans. Furthermore, the banks lead in savings, discounting bills and agency functions among others. The commercial banks have been structured through well framed regulations. It is an intensive sector serving approximately 47Million people in Kenya. However, Nigeria serves more than 200Million people (Baik, 2019).

The commercial banks are very important in Economic development of the country. Earning quality is very paramount in the commercial banks. It provides the credible and reliable financial information. The financial well-being of commercial banks must be addressed through proper earning quality and leverage. The conformity to the CBK's rule and regulation is a key forward-looking step (Muthuri, 2019).

1.2 Research Problem

Dechew & Dechey (2002) illustrated that liquidity was inversely associated qualitative financial reports. Earning quality portrays the true state of the company's financial health. It analyses the previous revenue and comparison with the subsequent earnings to gauge the future. To reach at earning quality free from manipulations, the company must provide full disclosure of their earnings. Leverage provides the true position of liquidity and solvency while earning quality provide an overall financial health.

Commercial banks in Kenya must adhere to accounting principles to enhance their earning quality. Leverage of commercial banks portrays the sensitivity of financial variables. Leverage and equality are good for the

prudent financial stability. The debt-equity ratio is very important to the shareholders and investors. It is used to determine the liquidity and solvency of the firm. Commercial banks serve many people through deposit taking, loans advancement among other critical roles (Muthuri, 2019). The ability to remain competitive enhances their profits, innovation and creativity. The financial statements must promote objectivity and consistency to realize the going concern principle (IFRS, 2015). The public can be the greatest financial statement in knowing the well-performing firms which they can invest in.

Hassan & Bello (2013) concluded that leveraged companies have great likelihood of increasing revenues if the best control measures are put in place. The research used correlation design. Leverage and Earning Quality are paramount in the commercial banks. Leverage determines the best capital structure that enhance net present value. It presents the true and fair financial state of the firm. It assists the investors in technical and fundamental analysis. In nutshell, it is a fundamental tool, predictive and increases the ways of attaining the purpose of the organization (Yusuf, 2020). Leverage can quantify the alternation in revenues and help the governance in cost regulation and projections. Equality ensures the financial statement are presented in full adoption of accounting principles.

The driving force for this research is the proposition that leverage is the fundamental factor affecting decision making process. The corporate governance may manipulate their decision to portray a good picture to the economic users. The objective of manipulation is driven by the organizational desires as well as personal targets. The previous researchers have focused so much on the leverage or earning quality and financial performance of the companies. Yusuf (2020) concentrated on the effect on earning quality on the market value of the firm. The researcher concluded that earning quality has positive association with market value. Hassan & Bello (2013) studied profitability and earning quality and concluded that profitability had positive association with earning quality. Shivakumar (2005) focused on quality of financial reports of private companies and found out the positive association. The research undertaken previously have use sampling method and focused on other sector of economy apart from the commercial banks. The researches have been undertaken long time ago cannot stand in the current business environment due to technological advancement and emergence of new methods of businesses. Furthermore, the research undertaken in specific region or globally cannot be generalized to portray the Kenya set up due to different macroeconomic factors, business environment and guiding legislations. In a nutshell, there is no study that has focused on the

leverage and earning quality of the banks. The study will try to answer numerous questions that come up alongside leverage and earning quality. The question that arises daily is: What is the effect of leverage on earning quality for the commercial banks in Kenya?

1.3 Research Objective

This research seeks to assess the effect of leverage on earning quality for the commercial banks in Kenya.

1.4 Value of the study

The study is very integral in the banking sector of Kenya since they will get more information on the leverage and earning quality of the commercial banks in Kenya. It will build the foundation of knowledge for more researchers and scholars. The information obtained will be useful and indicative of the future projections.

It will benefit the student through provision of insight information, valuable analytical skills, and in-depth knowledge. It reinforces the theories and the principles advocated under accountancy. It builds capacity for futuristic references. It solves the problems facing commercial banks' financial reporting.

The policymakers will use the research for their robust and integral policy formulation. In summary, the research is very important to shareholders, investors, and government in obtaining financial information for both technical and fundamental analysis. Leverage and earning quality are useful in investment decision making.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter covers the far-reaching review of how leverage affects quality earning among the commercial bank in Kenya. In ensuring the success of this literature review, an understanding of what leverage is and its relationship to quality earning is first put across. The language and tone used is formal yet more to the point to review topic. Then, the theories surrounding leverage in the commercial banks in Kenya including their determinants is explained. Empirical studies help in illustrating the facts and information in a more elaborate way. A clearer image of the review question is best presented in the form of a conceptual framework. Lastly is the summarized literature reviewed and conclusion after the above steps.

2.2 Theoretical Review

Majorly there are three key theories that effect leverage on earning quality among the commercial banks in Kenya. Categorically and by virtue of mention they are, trade-off which clarify on the debts and earning quality, pecking order demonstrate the capital structure, and agency theory.

2.2.1 Trade-off Theory

Modigliani & Miller (1958) initiated the theory based on the perfect market assumptions. The theory is grounded and established on the relationship between debt finance, equity finance, tangible assets, and intangible assets. In a case of massive tangible assets then debt finance is used, while massive intangible assets apply in the case of equity finance. That suggests that the operations commercial banks should ensure ideal debt-equity ratio according to al-Tally (2014). Comparisons from cost relating to debt-finance, determine the ideal debt amount alongside the benefits from the debt-finance. That suggests there is massive leverage to finance investments in a more profiteering bank. In reference to the theory, most banks have to ensure equilibrium in tax advantage utilization of leverage alongside costs, hence, linking to application of leverage as a way of investment in the bank (Aliu, 2010).

The theory emphasizes on the positive association that exists between leverage and earning. This preposition has been proven wrong empirically. The assumptions of theory that there is no transaction cost is unrealistic. Furthermore, it does not consider the distress cost and transactional expenditure. The assumption cannot stand in the real financial world.

The theory holds that banks can only borrow to the magnitude, when the tax-shield on debt funding can immediately compensate the total costs related with debt funding (Itiri, 2014). For the above condition to be fulfilled, firms have to borrow from commercial banks gradually in such to reach equality in optimum ideal debt- ratio level. Then the firms have ability to reach maximum market value that will alleviate debts from funding, the firms can be said to have benefitted from the funding (Bontempi& Golinelli, 2001). The theory assumes that there is no floatation cost, buying and selling does not involve transaction cost. Furthermore, it states the absence of taxation this not applicable in the real financial world. There is usually transactional cost on purchase of securities, moreover, there presence of taxation in the market.

This theory is essential to both commercial banks and the firm acquiring financing from the banks in that it suggests easier access to financing and easier paying within the optimum time allocated.

2.2.2 Pecking-Order Theory

Origin of this theory dates back to several years (Myers &Majluf, 1984). Propositions of the theory operate on the principle that businesses follow a preferred way of financing their decisions. Companies raise their value by funding their assets or resources. It also explains the results emanating from asymmetrical information existing between external and internal of the company (Bitok et al., 2011). However, there underlying asymmetries information amid the management of the specific company and the overall buyers, the buyers have a likelihood to underneath valuation of the firm's new stock that has been showcase in the market. To avoid such a scenario, firms use their own internal economic assets to fund investments and

processes. Whenever the internal assets of finance are not sufficient to fund the investments, then the company can spearhead the debt-financing strategy. The scenarios whereby debt-financing is no longer beneficial for the company (fees related to debt financing are greater than the profits of debt funding), the company can do problem fairness through stocks (Raza, 2014). In simpler definition, this concept proposes protocols and procedures in funding initial projects, major companies may prioritize to finance with inner resources, observed by means of using debt then equity (Al-tally, 2014).

The principle of pecking order indicates most appropriate capital shape is non-existent considering that debt ratio occurs due to aggregate external funding mandatories for this reason the prime determinant of a capital dynamic of a corporation is the cause of uneven statistics (Itiri, 2014). Essentially, this principle advocate that corporations will use debt in place of fair share to finance its investments (Nyamita, 2014).

Pecking theory fails to recognize there exists goal-leverage: wherein retained profits is the initial priority in funding preference and fairness, this indicates that stocks become the last resort (bontempi & golinelli, 2001). There are some weaknesses in this Pecking Order Theory. The theory does not consider the effect of existence taxations and instead look at the different picture from the ideal market, the cost encountered on issuing new securities and the financial distress that is associated with management. Moreover, it fails to investigate the agency cost that is indispensable in the business environment.

The theory of pecking order is primarily reinforced by preposition that choices on the leverage use are catalytic agent to uneven information amid management of a firm and traders. However, theory fails to incorporate the presence of taxation and cost incurred or expenditure. Furthermore, it does not recognize the financial distress which is very possible in every firm.

The corporations anticipate cases where investors' perspectives may foresee the problem of equity in a pessimistic way. In that case, companies fund their projects through undistributed earnings as inner supply of

fund first, accompanied by debt and thereafter, equity as last resort whenever the primary alternatives fail to reach the fully indispensable budget for project (calabrese, 2011). The theory additionally recommends that several corporations with great level of economic desires will possibly become a totally awesome debt ratio whenever there is a consideration that managers do not opt for the difficulty of new.

2.2.3 Agency theory

The theory was opined and brought into being by Stephene & Mitnick in 1970. Later on, in 1976 Jensen and Meckling advanced the theory. It proposes a condition when firms' managers and stakeholders fail to manage their own businesses (Jensen and Meckling, 1976). Managers are entrusted since they are the agents of the shareholders, however the management can culminate pursuing their egocentrism at the cost of the corporate shareholders. This results to an agency tussle. However, it is resolved through numerous approaches like ownership structures, audit management and surveillance.

However, theory does not consider the agent who are under duress in making decision. This is possible in the situation when the principal wants illegal and unfounded decision that can sink the firm to economic oblivion. The theory considers the principal as a key decision maker and cannot address the key policies being formulated by board of directors, corporate governance, and top management. It should focus on the stakeholders and come up with best decision instead of being subjective.

The management relied on deciding on behalf of the principal thereby shaping the firm's characteristics of an organization. For example, they decide on level equality of a firm. Additionally, the initiatives should have enough capital to bare the potential losses from financial depravity. The 2007/2008 finance crisis that came in the backdrop of excessive loaning commercial banks was mostly from company's management decisions within the banking sector (Calabrese, 2011). The bank's administration also makes liquidity control decisions which influences the overall banking processes and at large their operations. Resolutions

on asset worth relies on management to come up with them. The management has to take into account investors' wealth in their decision-making process. Other times, the management is allowed to come up with other considerations. For example, the management may choose to consider extreme leverage and misappropriation of funds raised to target risky ventures that could lead on to huge loss of investors' wealth.

2.3 Determining of financial performance

Corporations have other objectives rather than raising shareholders' value which is primarily achieved through maximizing their profit. This performance is measured in terms of profitability which in turn is evaluated from corporation's revenue to costs linked to generating revenue. Factors that determine profit and financial success to commercial banks are numerous in nature. They include size of a corporation, credit rick control, leveraging levels and the interest rates involved. Below a deeper insight into each one of them.

2.3.1 Degree of Leverage

The effect of leverage on economic prosperity of corporations continues to be mind-boggling in finance literature field. Numerous students have varying perspectives on the subject and there's no one stand on whether leverage influences on both extreme contrary sides on an organization's economic performance. Modigliani and Miller (1963) argue that there's a bonus on gearing because of tax shield that results from tax deduction of recreational, benefit is cumulative; the greater pretty geared a business enterprise is the greater tax ease it receives and the better the organization price because of decreased prices. Agency fees concept additionally helps the proposition that excessive leverage ends in higher economic performance.

The idea shows that organizations with excessive profitability, managers can also misuse the organization's assets for his or her personal character benefits. As such, use of debt is used a disciplinary degree to lessen the scope of managers by decreasing allocation to managers thus ensuring they show greater responsibly and therefore reduces business enterprise prices. Therefore, excessive leverage is expected to lessen business

enterprise costs, lower ineffectiveness, increase efficiency, and facilitate growth in the organization (Akintoye, 2008). In contrast, Brigham and Gapenski (1996), nevertheless, keep that the insolvency costs should portray a trade-off amid debt and equity. Counting on an excessive amount of debt, pretty leveraged corporations incur economic misery cost. Financial misery prices consist of prison costs, lack of tax shield, accountancy costs and administrative prices which lessen the income margins. Therefore, in line with this proposition, there's a bad affiliation among leverage and economic performance.

2.3.2 Bank Size

Corporation's profitability and liquidity are affected by the organizational scale. Larger enterprises eventually have a wider market share hence translates to most likely, greater profitability (Brav, 2009). Though there is unclear definition of corporation size, it is often classified with increase in assets, returns amount, production capability and variety of produced products to consumers. Through this idea huge corporations are able to produce high quality products at lower costs compared to small corporations.

More modest corporations have a higher likelihood of insolvency since they are more enhanced when contrasted with more modest firms. Consequently, bigger firms absorb more obligations as they pursuit to reduce insolvency costs. Greater relations can limit information unevenness on the lookout and the gain monetary assets productively (Pardron et al., 2005).

2.3.3 Efficacy of the management

Management efficacy is evaluated in terms of overall asset growth and earned flow. Management efficiency as measured by total asset growth, business development, and profit stream is supreme yardstick that portrays the financial performance of the business. Management efficacy promotes growth and sophistication. Furthermore, it enhances innovation, accomplishment of strategies and inspires imitative.

The best-growing companies improve financial performance, especially when the magnitude of total assets escalates, thus indicating that higher growth and tends to obtain higher profits (Sekerci, 2013). Financial ratios, such as the operating profit-to-income ratio and the operating expense as a percentage of total assets, are useful in evaluating management efficacy. The effectiveness management encourages optimum growth and substantial development.

2.3.4 Fluctuating Interest Rates

The fundamental origin of income for business banks is revenue on client advances while their greatest expenses are revenue paid on client stores (CBK, 2017). Banks make benefits by keeping a range between revenue charged on advances against revenue paid out on client stores. Frequently, the premium charged on credit is a typically at higher rate contrasted with the interest paid on the clients' stores. An increment on financing cost expands the incomes acquired by the bank in type of revenue on credits. Investors likewise procure more when loan fees rise and as such expenses for the banks rise.

Banks charge revenue dependent on a client's risk profile. The spread between loaning financing cost a lot on stores decides the benefits. Continuously, banks charge an incremental pace of revenue on credits than they impose on stores thus a build out on loan fees decidedly, impacts implementation of banks through enlarged incomes, contrary to a more modest increase in the expenses (Abubakar, 2015). In 2016, the CBK presented loan cost cap where the loaning rate is covered at CBR rate in addition to 4% and a base revenue on stores at 70% of CBR. The CBR is at present at 10.5% subsequently loaning financing cost is covered at 14.5% and financing cost on stores basically at least 7.35% (CBK, 2017).

2.3.5 Credit Risk Management

Credit risk is an important aspect in securing loan, as such banks face credit risk. The credit risk occurs if the borrower is available for the loan payment contract. The creditworthiness, the health and profitability of the

Bank is in danger, specifically if the credit risk is high because of malfunctioning loans. Therefore, commercially available banks are important to monitor asset quality indicators through the monitoring of particular risk trends, especially in the trend of certain risks. The borrowers with the default payment for the reimbursement of the loan is faced with cache flow problems and is negatively affected along the liabilities of said position and cash profitability.

2.4 Empirical Studies

Rajkumar (2014) did research on the influence of financial leverage on financial success. The case study was John Keells Holding Public Limited Company of Sri Lanka and utilized a 7-year data running from 2006-2012. The research scrutinized the association amid the financial leverage and financial effectiveness. The study optimized the correlation analysis. Furthermore, regression analysis was conducted to determine its relations. A negative relationship and was found amid the predictor and predicted variables. However, the study cannot be generalized since it focused on only one company.

Enekwe et al (2014) did research with a purpose of scrutinizing the association amid financial leverage verses financial performance. The area of concentration was Nigerian-listed pharmaceutical companies. The study utilized ex-post research design. Furthermore, the research incorporated correlation for easier interpretation and multiple regression to analyze the data. The period run for 12-year financial reports covering 2001-2012. The resulting findings concluded on insignificant effect amid predictor variable and predicted variable. The research years of coverage were long enough to give conclusive findings. However, the research was conducted on six listed companies hence too small to represent the whole population.

Abubakar (2015) studied the financial leverage and financial productivity of Nigeria Banks. the study sampled eleven deposit-taking banks and had 9-year period starting from 2005 to 2013. Regression analysis showed the existing association amid debt-equity and ROE. The explorative studies must be done on the other ratios to reach at very important conclusion.

Zahoor et al (2020) conducted a study amid financial leverage and performance. The study was carried out in Pakistani companies. The objective was to evaluate the effect of financial leverage on effectiveness of companies in Pakistan. The research was conducted on 154 textile companies quotes in Karachi Stock Exchange covering 6years from 2006-2011. Descriptive statistics was utilized. Furthermore, multiple and correlation analysis were utilized to provide linkage between the predictor and predicted variable. The results showed a negative link amid leverage the performance. The study was big enough to arrive at conclusive results, however similar studies should be conducted in other regions.

Mohammad (2014) studied the association amid financial leverage and financial success of publicly traded chemical companies (Pakistan). Data covered 20 dating organizations from the KSE Chemistry Department were used for an 8-year period from 2006-2013. The research optimized descriptive statistics for accuracy and overall overview, correlation to seek association level, and regression to achieve the research objectives. The research results showed the positive correlation between ROA, net profit margin and ROCE and debt-to-equity ratio, while there is a negative correlation between ROE and debt-to-equity ratio. The debt verses equity ratio is the only leverage indicator used. Other coefficients, such as debt ratio and long-term debt ratio, need to be tested in similar studies.

Arif (2020) did research on EQ and market value. The study concentrated on firms listed in NSE. The research descriptive research design, regression, and analysis. The study concluded that by enhancing accruals quality, it leads to improve in the market value. However, the study cannot be used to generalize the commercial banks in Kenya hence need for research.

Chepkwony (2018) investigated how earning management was influential to the stock earnings of NSE quoted firms. The objective was to evaluate how earning management is crucial and impacted on stock performance. The research optimized the descriptive design for the period running from 2013 to 2017 for the

companies that were stagnated. Multiple regression was used in the methodology. The research findings indicated a positive insignificant effect of earning management on earning quality.

Gworo (2019) researched on the relation between volatile earnings and the intrinsic value of NSE Companies. Correlational design was paramount in the study of 30 firms quoted in NSE. The study utilized already available secondary data that covered 2011 to 2015. The findings show a positive impact on the value of companies. The research indicated that the higher the volatile earnings the higher the market value and vice versa.

Ngunjiri (2017) concentrated on the relation between amid management and firm's performance quoted in the NSE and tried to evaluate if earning management had an association with financial performance. The study used descriptive method, census, and ordinary least square data analysis. The findings opined that earning management had a positive relation with ROA.

Amenya (2015) undertook research amid association of capital composition and financial efficiency of NSE's listed firms. The companies composed of 26 from 61 firms and the research cut across 2008-2013. The research utilized descriptive design and optimized the secondary data. Furthermore, it incorporated correlation and regression analysis to reach a conclusive finding. The study portrayed negative correlation.

2.5 Conceptual Framework

The study seeks to assess the impact of economic leverage on economic overall earning quality of non-financial corporations indexed at commercial bank. The impartial variable became monetary leverage even as the manipulate variables have been organization length an organization liquidity even as the reliant variable will be overall banking performance.

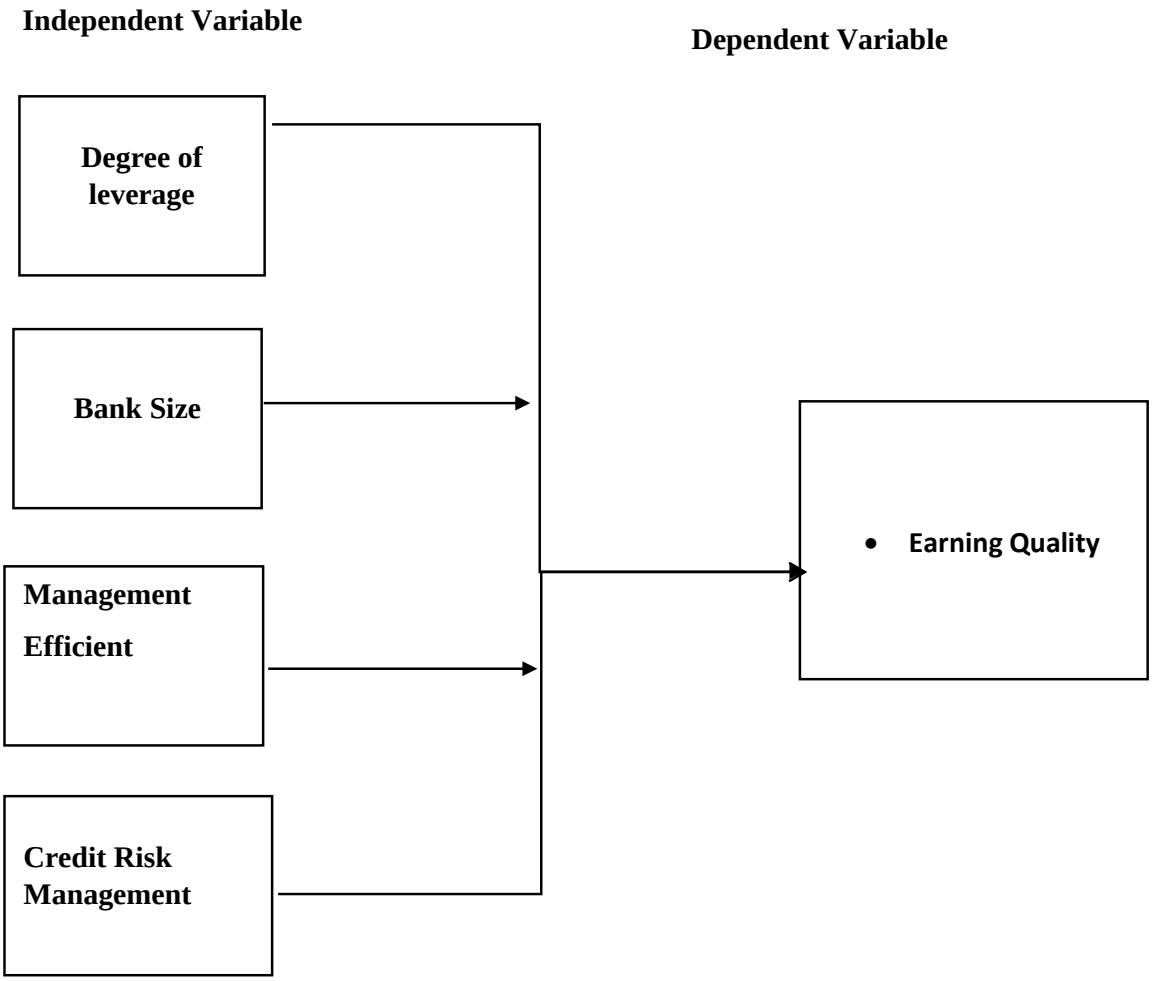


Figure 2.1: Conceptual model (Source: Researcher, 2021)

2.6 Summary of Literature Review

This section summarizes all the concepts surrounding countless empirical studies on the impact of leverage on earning quality among commercial banks. Research by Adenugba, & Kesinro (2016) illustrated the significant impact of leverage. Furthermore, Maghanga and Kalio (2012) concluded that financial leverage has a significant impact on leverage. Leverage is paramount building shareholders wealth and quantifying the proportion of changes in profits. It portrays a picture of the companies' going concern.

Syed et al. (2015) demonstrated that leverage helps in forecasting. Enekwe, Agu and Eziedo (2014) postulated that leverage boost efficiency. Raza (2013) indicated that leverage is paramount is building

wealth. Banafa (2015) have shown that financial leverage does not have a significant influence on leverage, while Rajkumar (2014) determined that there is a negative correlation between financial leverage and financial performance. Gweyi and Karanja (2014) proved a positive correlation amid financial leverage and profitability. Saying of this review studies, the relationship between financial leverage and corporate performance has been analyzed, which differs according to the corporation and the country in which the research institute is located.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter is very much crucial as it carries the research structure. The entire research is divided into six portion or steps that systematically explains the research process. Firstly, it is the research design, then population, followed by sample design, data collection, its integral analysis and finally the diagnostic steps.

3.2 Research Design

Research design is the capstone of the whole research process (Yin, 2009). Just like in a building it shapes the whole research process by providing how to gather data, measure it and then to analyze it (Bryman & Bell, 2007). If the research methodology is inconclusive then the issue lies with the research design. Research design determines the logicality, concise and importance of the research methodology in a research project (Thomas, 2010). By doing so the research question are answered amicably.

Among the many methods of research such as, qualitative research, quantitative research, the researcher chose to use descriptive research design method. The factual reason being descriptive design points at enlightening on the various aspects of the research question (Thornhill, 2009). It also offers information about turn of events that concerns the research (Bryman & Bell, 2007).

In descriptive analysis, a probe into population that provides the data is factored in during its measurement. Descriptive studies targeted at providing a narration of phenomena. The study analyzed the distribution pattern, specific population in singularity point in the period (cross sectional) or comparatively over time (longitudinal) by utilizing repetitive surveys (Rose, Spinks and Canhoto, 2014).

3.3 Population

The population compose of group of people or entities that exhibit synonymous characteristics to the study thus can be used to generate inferences. This research maximized the population of forty-two commercial banks 2016-2020.

3.4 Data Collection

This research collected data from the examined, printed financial magazines and publications concerning the commercial bank of Kenya. The secondary data was also sourced from secondary methods especially the publication on the CBK website and their journals. Furthermore, Secondary data was also sourced from Kenya Bankers Association. Data for purpose of study was hauled from statement of financial position and statement of comprehensive income from 2016-2020. Moreover, the data was be mined from the Commercial banks and Capital Market Authority website which was then observed and thereafter the generation analysis.

3.6 Data Analysis

This research methodology utilized numerous regression study and association analysis to evaluate the connection existing between effects of leverage on earning quality among commercial banks in Kenya. Level of effects from leverage on earning and quality was the proportion of influence while corporation size and non-performing advances proportion were the control factors estimating size and credit control procedure by that order. The importance of the relationship was ascertained by a 95% certainty level. The information was likewise investigated utilizing descriptive insights proportions of mean, middle and standard deviation.

3.6.1 Diagnostic Tests

Diagnostic Tests that were undertaken in this study include linearity, normality, autocorrelation, and multicollinearity. Linearity was presented through scatter plot and normality used Kolmogorov-Smirnov

Test, Autocorrelation was obtained through Durbin Watson test and Multicollinearity by the use Variance Inflation Factor. The ordinariness was needed to coordinate single or joint speculation tests concerning the model boundaries. Ordinariness test used in utilizing skew and Kurtosis test.

The unitary root test utilized Fisher-Type Test to set up whether the factors were fixed or non-fixed. The reason for this is to stay away from misleading relapse results being acquired by utilizing non-fixed series.

Multi-collinearity is inspected in the exploration utilizing the change inflation factor (VIF) whereby there will be removal point for outrageous multi-collinearity (Katrutsa and Strijov, 2017). Impeccable multi-collinearity results into questionable backslide coefficients and huge standard blunders while the closeness of insufficient multi-collinearity results into enormous standard mistakes. Huge standard blunders sway the exactness and precision for removal or inability to dismiss the invalid speculation

3.6.2 Empirical Model

The various relapse condition model that utilized for this examination

Resnik (2003) indicates the importance of the model in the data analysis.

An empirical model was utilized to portray a linear association for the variables under the investigation.

A regression model shown below

$Y=\alpha_0+\beta_1X_1+\beta_2X_2+ \beta_3X_3+ \beta_4X_4+ \varepsilon$

Whereby

Y= Earning Quality (Measured by accrual quality)

A_0=y intercept of the regression. The constant variable.

X_1= Degree of Financial Leverage (Total debts as a percentage of total assets)

X_2= Bank Size (Calculated as natural logarithms of the total assets as per CBK)

X_3= Management Efficiency (Total sales as percentage of average inventory)

X_4= Credit Risk Management (Debts as a percentage of income ratio)

ε= error term

3.6.3 Significance Tests

The relapse model aided in deciding whether there was a connection between leverage and earning quality of commercial banks. ANOVA test was utilized to find out the effect of leverage on the earning quality.

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter is paramount in the analyzing data, results presentation, crucial interpretation as well as reinforcing the discussion. The analytical descriptive analysis and regression method. The data were collected from Central Bank of Kenya, Capital Market Authority, and the banks. The research sought to assess the effects of leverage on earning quality among commercialized banks in Kenya. The data was collected spanning from the period of five years from 2016-2020. The descriptive and regression method were undertaken to provide a holistic perspective.

4.2 Descriptive statistics

This part shows us results of the descriptive characteristics of data analyzed over five-year period. The table below shows descriptive summary of the variables that was obtained from the analysis.

4.2.1 Summarized Statistics

The descriptive statistics shows that earning quality had a mean of 9.02 with a standard deviation of 15.91. It also had a maximum earning quality of 37.49 and a minimum of 1.6812 indicating that there has been a significant difference in financial performance of the Kenyan Banks because of Leverages.

Table 4.1: Summarized Statistics

	Earning Quality	Degree of financial leverage	Bank Size	Management Efficiency	Credit Risk Management
Mean	9.02678	81.8942	2785.82	79.336	2023.333
Standard Error	7.116847713	1.821998	4.277998	2.862208	0.701708
Median	1.907	82.011	2783.44	80.11	2022.714
Standard Deviation	15.91375527	4.074112	9.565895	6.400092	1.569066
Sample Variance	253.2476068	16.59839	91.50635	40.96118	2.461968
Kurtosis	4.994104177	1.269924	-1.21534	0.923788	-1.88178
Skewness	2.234437128	-0.04149	0.600647	0.625008	0.665226
Range	35.8088	11.302	23.37	17.21	3.63
Minimum	1.6812	76.209	2775.83	71.71	2021.846
Maximum	37.49	87.511	2799.2	88.92	2025.476
Sum	45.1339	409.471	13929.1	396.68	10116.67
Count	5	5	5	5	5
Confidence Level	19.759537	5.058678	11.87763	7.946764	1.948253

(95.0%)					

Degree of Financial Leverage had a mean of 81.89, a standard deviation of 4.074112. Its minimum was at 76.209 and its maximum was at 87.511. This, therefore, indicated that for every change in leverage, working income for all Kenyan bank's changes by 81.89 times. Bank Size measured as total assets had the highest mean of 2785.82 with a standard deviation of 9.56, Maximum of 2799.2 and minimum of 2775.83 implying that Kenyan Banks are close in size.

4.3 Correlation Analysis

This was necessary to help in testing the degree of association amongst the variables. See the table below, it shows the correlation analysis.

Table 4.2: Correlation analysis

	Earning Quality	Degree of financial leverage	Bank Size	Management Efficiency	Credit Risk Management
Earning Quality	1				
Degree of financial leverage	0.01299	1			
Bank Size	-0.01899	0.999105	1		
Management Efficiency	0.075635	0.997982	0.994864	1	
Credit Risk Management	-0.02519	0.998872	0.99998	0.994237	1

From the table above degree of financial leverages has a positive correlation against earning quality. Bank size a negative correlation against Earning Quality and a positive correlation against degree of financing. Management Efficiency has a positive correlation against Earning quality, Degree of financial leverages and the bank size. The credit risk Management has a negative correlation against Earning Quality and positive correlation towards degree of financial leverages, Bank Size, Management Efficiency and the credit risk management.

The multicollinearity test above is important in that it helps to check weather two variables given are highly correlated. The correlation coefficient between two independent variables should not be greater than 0.7 otherwise the Multicollinearity test problem exists. In such an occurrence, greater than 0.7, one of the independent variables should be omitted in the regression model.

4.4 Regression Analysis

This analysis tends to help us generate an equation to show the relationships between two variables. A multiple linear regression was done to establish the relationship between leverage and earning quality.

Table 4.3: Summary Output

Regression Statistics	
Multiple R	0.996407
R Square	0.992826
Adjusted R Square	0.98924
Standard Error	7.013171
Observations	13

The correlation coefficient, R, indicates the nature of the relationship between the variables. From this, we therefore conclude that there is a positive correlation 0f 99.64%. The coefficient of determination, adjusted R square, shows there is a variance level in the dependent variable change of 99.28%. The other 1.72% of profitability of this banks is caused by other factors that have not been captured in this research. This adjusted R Square value means that there is 0.000169 profitability change in Kenyan banks that is caused by Credit risk, Bank Size and Management efficiency.

Testing the Statistical Significance of the model.

Table 4.4: ANOVA

	Df	*SS*	*MS*	*F*	*Significance F*
Regression	4	54457.02	13614.26	276.7993	1.3165E-08
Residual	8	393.4765	49.18457		
Total	12	54850.5			

From the ANOVA table above the Significance level is 1.3165E-08. This value is less than 5% thus signifying that the data is perfect for deriving conclusion on the study variables. It also shows that bank size, credit risk and the management efficiency are significantly related to financial performance of Kenyan banks that have been listed.

4.4.1 Creating Model

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept (Earning Quality)	3.646157	3.099412	1.176403	0.27325	-3.5011005	10.79341	-3.5011	10.79341

Financial Leverages	-1.66779	4.642393	-0.35925	0.728704	-12.373167	9.037587	-12.3732	9.037587
Bank Size	3.171764	1.14071	2.780516	0.023906	0.54128068	5.802247	0.541281	5.802247
Management Efficiency	-0.11616	4.314613	-0.02692	0.97918	-10.065679	9.833352	-10.0657	9.833352
Credit Risk Management	-4.29088	1.583666	-2.70946	0.02668	-7.9428184	-0.63894	-7.94282	-0.63894

From this table above our regression Formula can be generated as below;

$Y=\alpha_0+\beta_1X_1+\beta_2X_2+ \beta_3X_3+ \beta_4X_4+ \varepsilon$

Regression of Coefficient=3.646157-1.66779 Financial Leverage + 3.171764 Bank Size -0.11616 Management Efficiency -4.29088 Credit Risk Management + E(error)

The Regression of coefficient would be 3.646157 if Degree of financial leverage, Bank size, Management efficiency and Credit risk management are held constant at zero. Degree of Financial Leverages, Management efficiency and credit risk management are negatively related to financial performance. while Bank Size is positively related to financial performance. A unit increase in Financial Leverages would result in a 1.67 decrease return on bank worth. A unit increase in Bank Size would lead to increase 3.17 increase in bank assets whereas a unit decrease in management efficiency would lead to decrease in return on bank value.

4.4.2 Linearity Test with Each Independent Variables

Degree of Financial Leverages

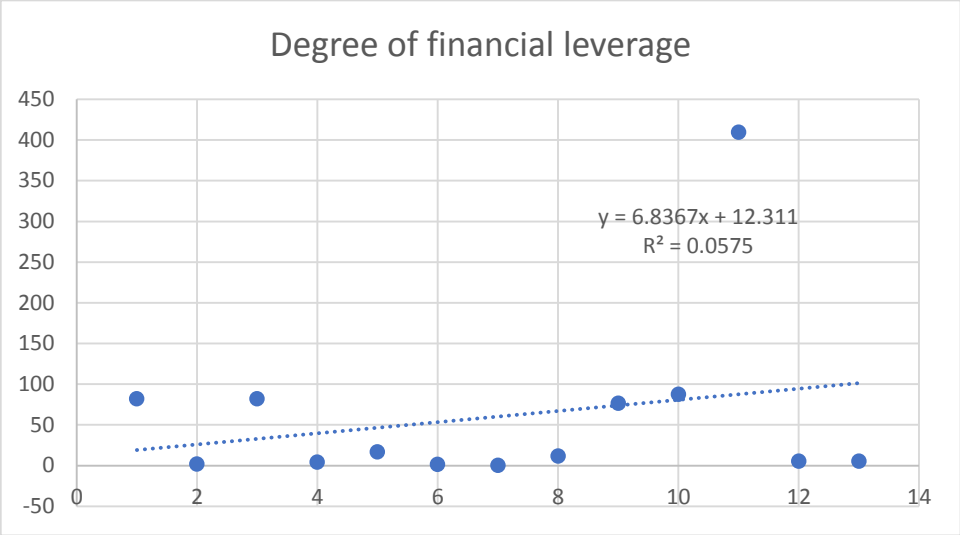


Figure 4.1: Degree of financial leverage

Bank Size

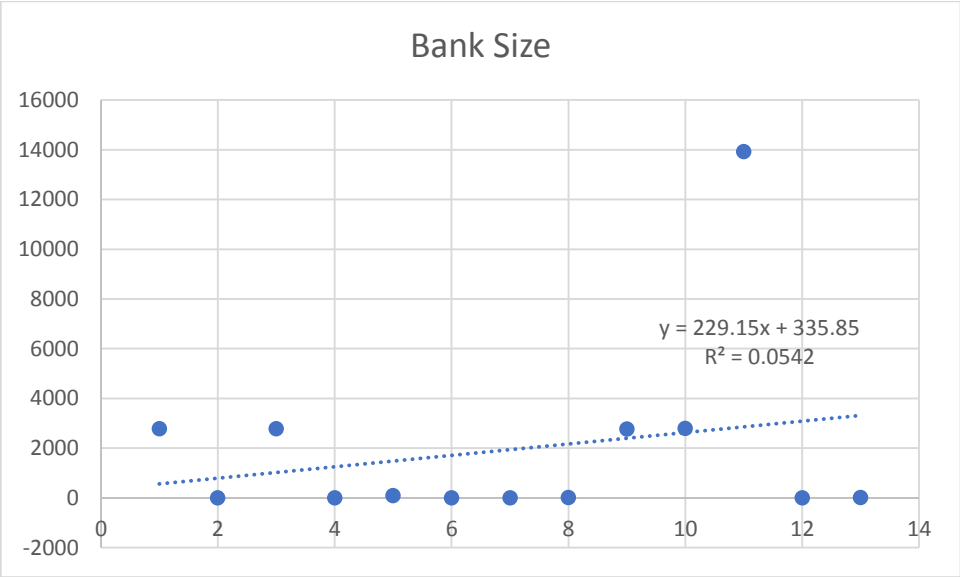


Figure 4.2: Bank size

Management efficiency

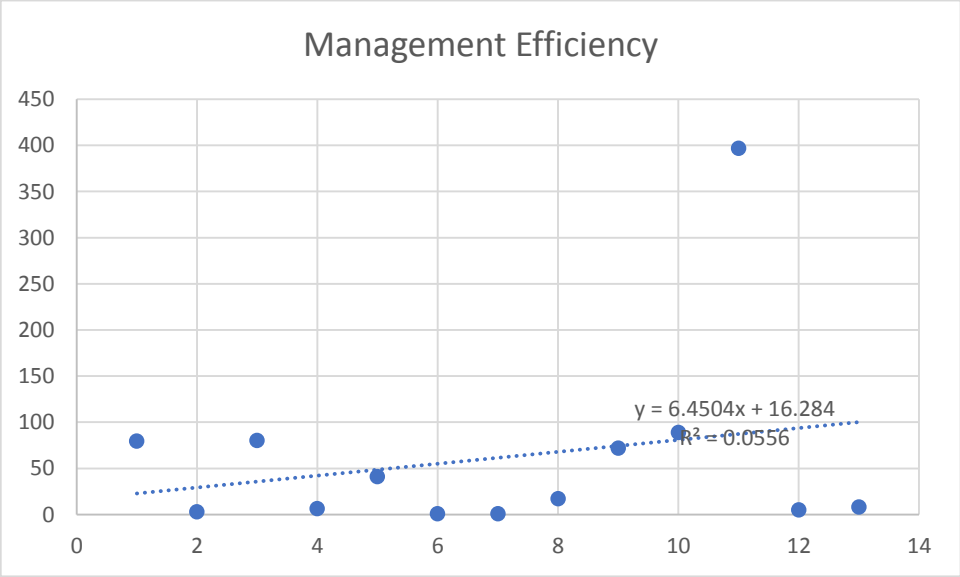


Figure 4.3: Management efficiency

Credit Risk Management

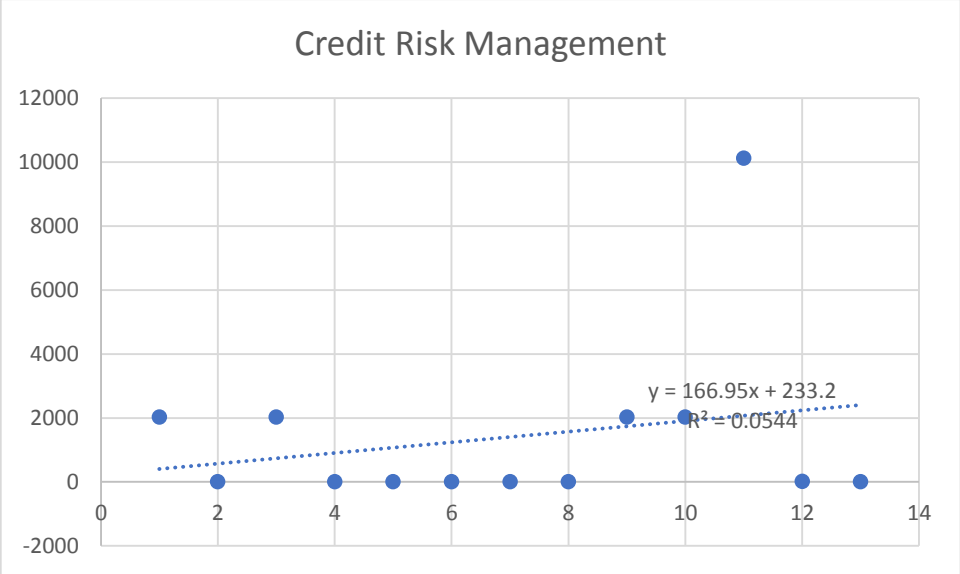


Figure 4.4: Credit Risk Management

Scatter Graphs

1. Earning Quality VS Degree of Financial Leverages

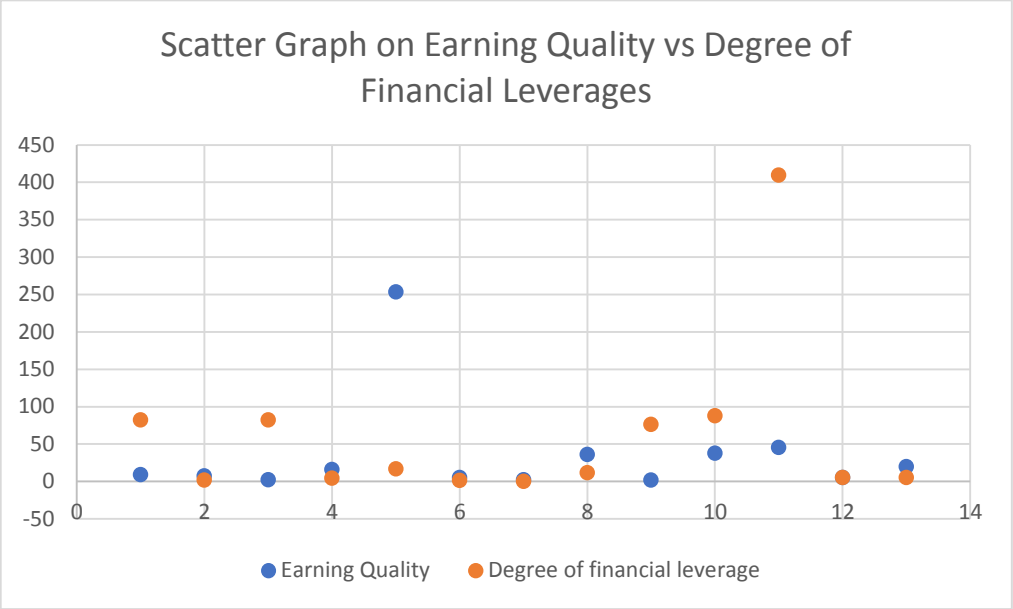


Figure 4.5: Scatter graph on earning quality vs degree of financial leverages

Earning Quality Vs Bank Size

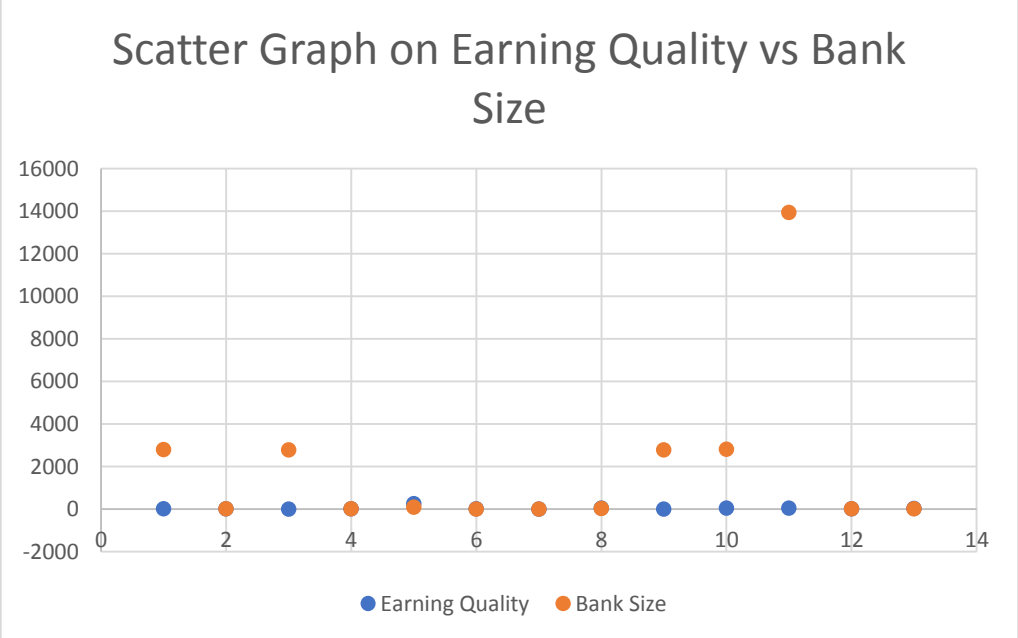


Figure 4.6: Scatter graph on earning quality vs Bank size

Earning Quality vs Management Efficiency

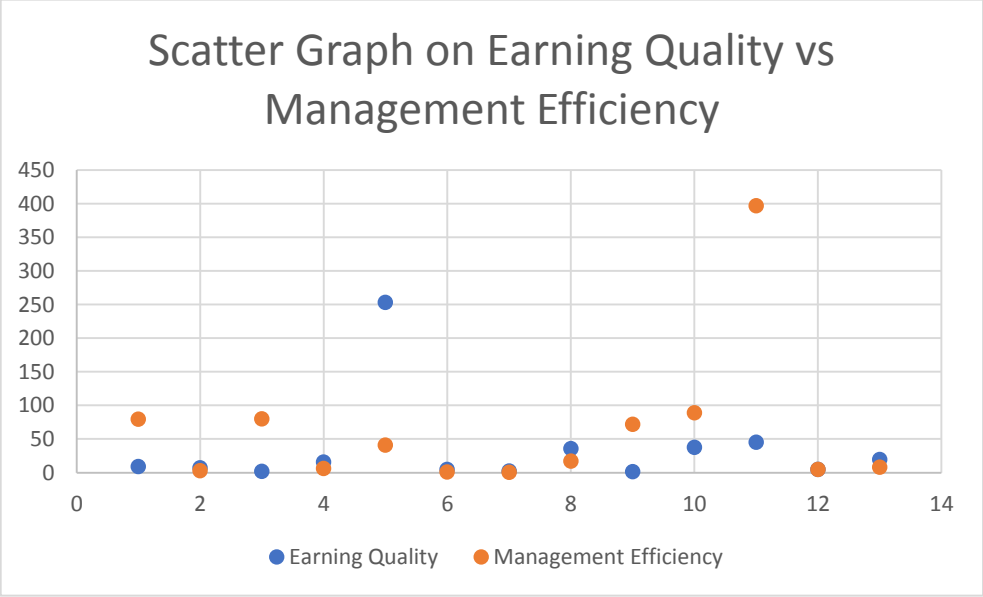


Figure 4.7: Scatter graph on earning quality vs management efficiency

2. Earning Quality Vs Credit Risk Management

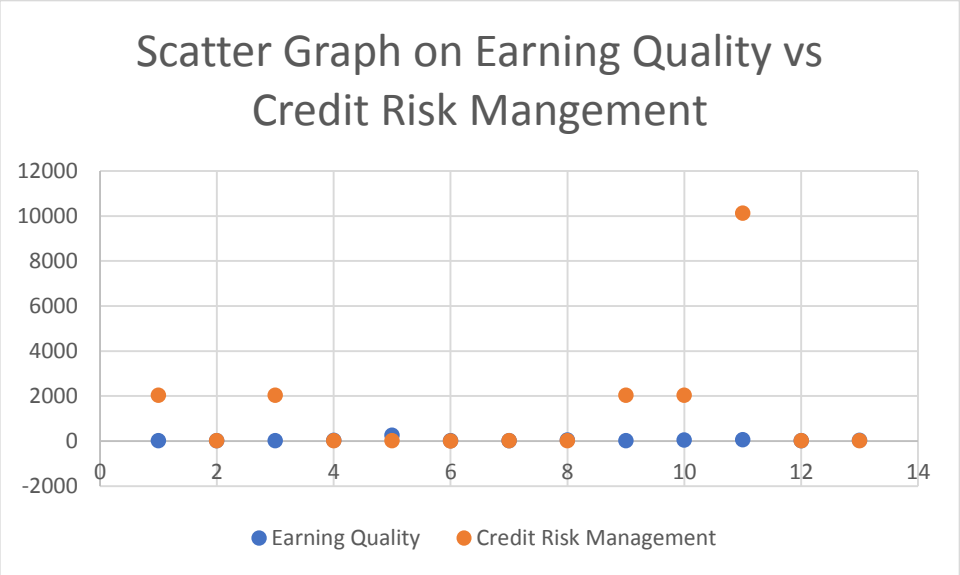


Figure 4.7: Scatter graph on earning quality vs credit risk management

From the above scatter graph, the level of association between the independent variables was within the normal range since it was below 0.7. The independent variables had weak association therefore no independent variable was eliminated.

4.4.3 Testing Assumptions

ANOVA[a]						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	53963.289	3	17987.763	213.288	.000[b]
	Residual	759.019	9	84.335		
	Total	54722.308	12			
a. Dependent Variable: Earning Quality						
b. Predictors: (Constant), Credit Risk Management, Management Efficiency, Degree of financial leverage						

From analysis of variance above, the processed data, had a significance level of 0.00. This therefore implies that a conclusion can be made from the study data since the significance level, P- VALUE, is less than the required 5%.

The significance was tested using alpha = 5%. The values were used in deciding the values

Coefficients of values. For every p-values less than 5%, H1 is accepted and for p-values greater than

5% fail to accept H1 and instead accept H0. The value in the above is 0.000 which is less than 5%.

Hence, at least one of the B is not zero. We fail to reject Hi. For the overall regression model, Fstatistic

values is compared with the corresponding critical values.

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B		Collinearity Statistics	
		B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
1	(Constant)	-.508	3.674		-.138	.893	-8.819	7.803		
	Degree of financial leverage	-13.858	1.733	-22.766	-7.994	.000	-17.779	-9.936	.000	5262.196
	Management Efficiency	11.818	.814	18.654	14.513	.000	9.976	13.660	.001	1071.996
	Credit Risk Management	.101	.040	4.166	2.508	.033	.010	.192	.001	1789.746

a. Dependent Variable: Earning Quality

4.5 Collinearity Test

Collinearity Diagnostics

Model	Dimension	Eigenvalue	Condition Index	Variance Proportions			
				(Constant)	Degree of financial leverage	Management Efficiency	Credit Risk Management
1	1	3.306	1.000	.02	.00	.00	.00
	2	.689	2.190	.61	.00	.00	.00
	3	.004	27.539	.25	.00	.09	.04
	4	9.571E-005	185.856	.12	1.00	.91	.96

a. Dependent Variable: Earning Quality

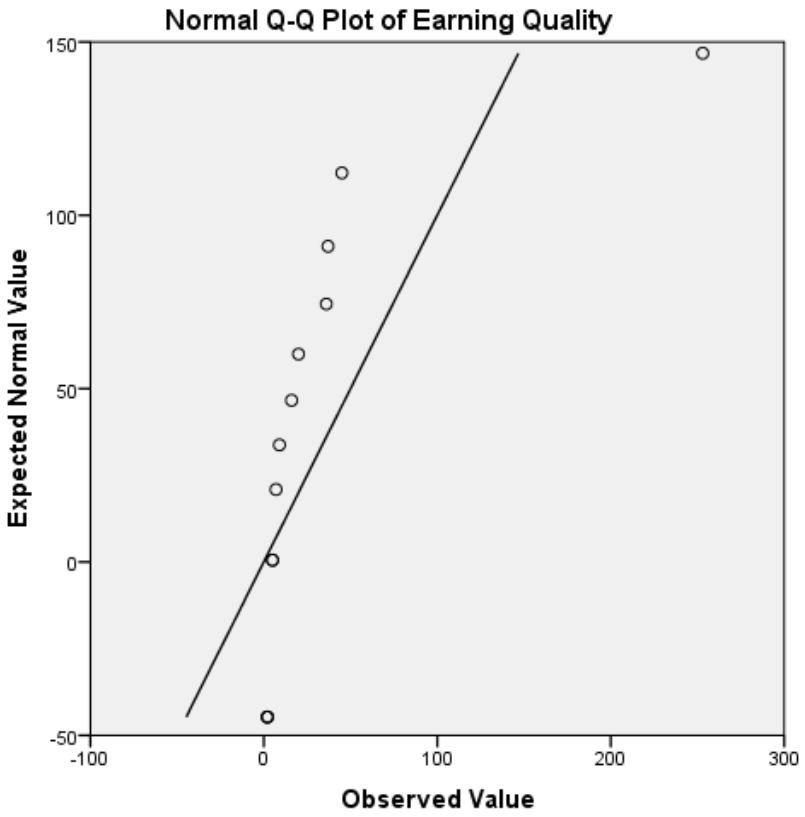
Residual Statistics

Residuals Statistics[a]

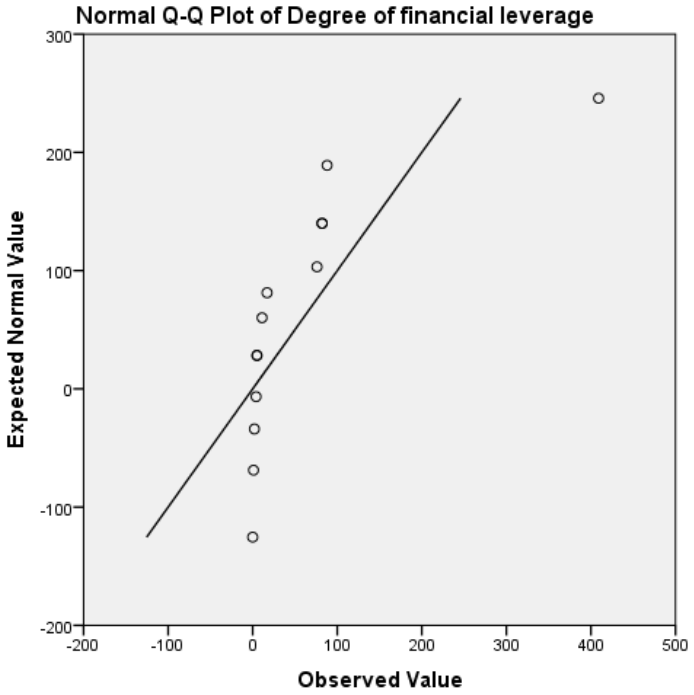
	Minimum	Maximum	Mean	Std. Deviation	N
Predicted Value	-10.20	248.64	33.77	67.059	13
Residual	-12.362	15.203	.000	7.953	13
Std. Predicted Value	-.656	3.204	.000	1.000	13
Std. Residual	-1.346	1.656	.000	.866	13

a. Dependent Variable: Earning Quality

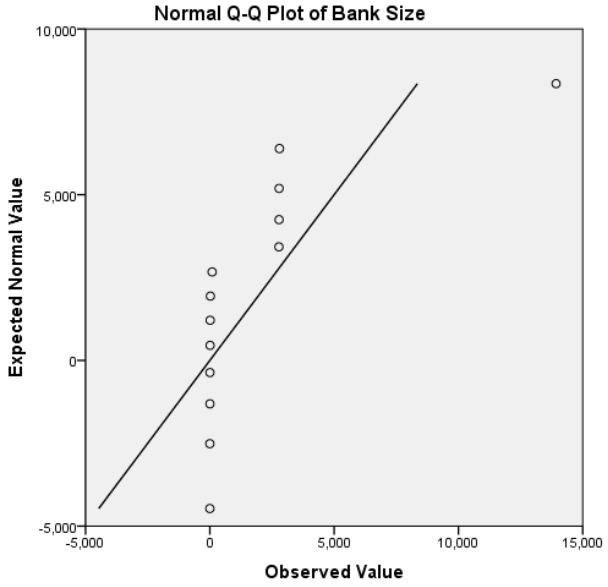
Normality Q-Q plots



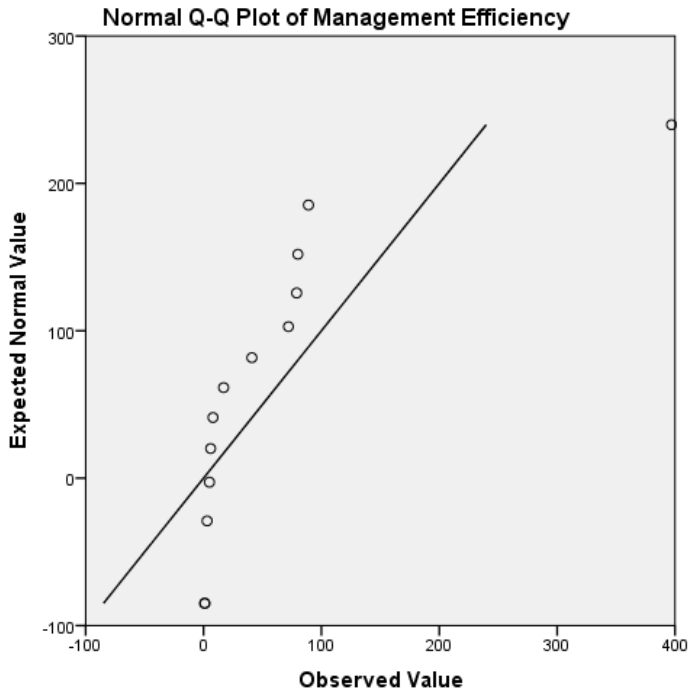
From the graph above it can be observed that the error terms are within the normal line with minimal insignificant deviations. Therefore, the error terms are normally distributed



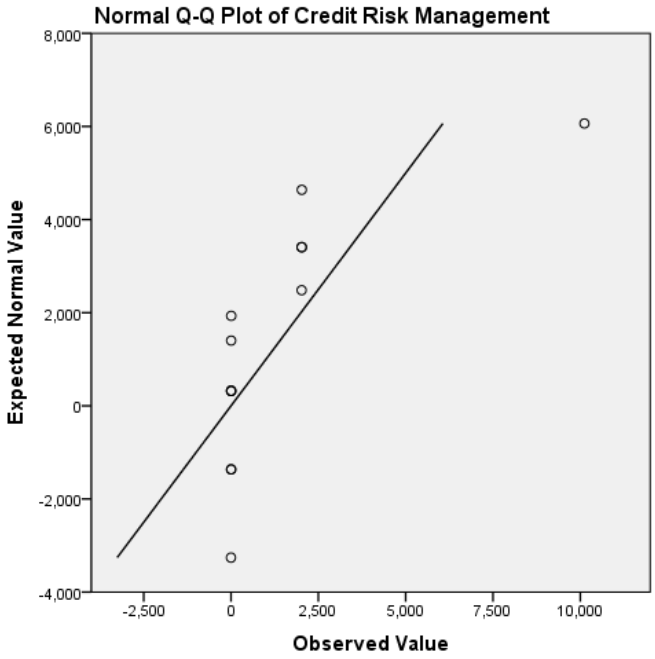
From the graph above it can be observed that the error terms are within the normal line with minimal insignificant deviations this implies that error terms are normally distributed



The graph above depicted that the error that was observed was not within the normal range hence but had maximum insignificant deviations. Hence the error terms are not normally distributed



The graph above postulate the observable errors terms was within the stipulated normal line hence insignificant deviations. This summarize that error terms was normally distributed.



It is well illustrated from the graph that the error terms were within the stipulated normal line. It had a very small insignificant deviation. This depicted the error terms are normal distribution. These reinforce the study of the independent variables.

4.6 Discussion of Research Findings

The research sought to investigate the effect leverage on the earning quality of commercial banks in Kenya. The research findings indicated that.

Earning quality=3.646157+ -1.66779 X_1+3.171764 X_2+-0.11616 X_3+-4.29088 X_4

$Y=\alpha_0+\beta_1X_1+\beta_2X_2+ \beta_3X_3+ \beta_4X_4+ \varepsilon$

Whereby

Y= Earning Quality (Measured by accrual quality)

A_0=y intercept of the regression. The constant variable.

X_1= Degree of Financial Leverage (Total debts as a percentage of total assets)

X_2= Bank Size (Calculated as natural logarithms of the total assets as per CBK)

X_3= Management Efficiency (Total sales as percentage of average inventory)

X_4= Credit Risk Management (Debts as a percentage of income ratio)

ε= error term

The research findings under the descriptive analysis resulted maximum of 37.49 and minimum 1.6812. The findings indicated that a change in one unit of earning quality, the constant value of 3.6462 while the degree of financial leverage will reduce by 1.66779 and bank size increase by 3.171764 while the credit risk management will decrease by -4.29088.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter is the cornerstone for the completion. It is crucial to conclude the analysis and recommend pivotal areas. The chapter present the finding that is holistic in the projected

5.2 Summary of Findings

The summary of the research is paramount in building the concrete pillar for the earning quality and leverage in the commercial banks in Kenya. The research incorporated the research objective. The study sought to find the effect of leverage on earning quality of the commercial banks in Kenya. The determinants scrutinized were degree of financial leverage, bank size, management, and credit risk management.

5.2.1 Degree of financial Leverage

The integral objective included the effect of financial leverage on the earning quality of commercial banks in Kenya. The research findings indicated that financial followed the normal distribution pattern. It had insignificant correlation amid the predictor variables including bank size, management efficiency and credit risk management. The result indicated an increase in the one unit of earning quality let to tremendous decrease in the degree of financial leverage by 1.6779. This is crucial indicator that earning quality and degree of financial leverage were inversely associated whenever the other factors were kept constant.

5.2.2 Bank Size

The study was determined to assess the influence of the bank size on the earning quality. The bank has been crucial in the determination of performance (CBK, 2020). According to ICPAK (2019) the size of the firm plays an integral part in the profitability and financial sustainability. This study assessed the bank size and found and the earning quality, the finding indicated that bank size had positive correlation with the earning quality. An increase by the one unit of earning quality led to an increase in the bank size by 3.1717 whenever all the factors are kept constant. This demonstrated the positive correlation and the movement in the same direction of both bank size and earning quality.

5.2.3 Management Efficiency

The management efficiency has obtained minimum consideration in the research. It has been one of the areas that has been recommended to be assessed. The research findings postulated absence of multicollinearity

amid the regressor variables. The findings postulated that whenever there was incremental of one unit of earning quality led to a decrease in the management efficient by 0.11616. This is contrary to the earlier finding by Ahmad (2016) which postulated that unitary increase in earning quality posted an increase in the effectiveness of management efficiency.

5.2.4 Credit Risk Management

The research assessed the credit risk management as one of integral part in the study of effect of leverage on the earning quality. The study was critical since it provided clear blueprint for the earning quality. The research was formulated an analytical model to stipulate the correlation relationship existing amid the credit risk management and earning quality. The research findings indicated that an unitary incremental of earning quality led to a decrease in the credit risk management by -4.29088 if all the factors kept constant.

5.3 Conclusion

The research findings indicated that degree of financial leverage, bank size, management efficient and credit management affected the earning quality. Earning quality was operationalized using the accrual quality. The research indicated both positive and negative correction amid the predicted variable. The study provided the great benchmark for prudential and comprehensive analysis. It provided the yardstick for the conclusive research findings.

The commercial banks should strive to promote earning quality and mitigate against the credit risk. The credit risk affects the earning quality negatively. The credit risk must be maintained at the very low level to enhance the earning quality. The bank size is crucial in the earning quality. The execution, planning and operational of banks must be supported by the robust management, and strategies for the going concern of the company. This research was the roadmap towards the conclusive research on the earning quality and leverage in the financial banks.

The Banks have bestowed tremendously and immensely to the economic development and growth. The banks acts as the agent of transformation, transaction, and foreign exchange. The banks have contributed to the milestone development of manpower while enhancing the productivity. The banks have stimulated the economic growth through the innovations and mobilization of the money circulation. The banks have

spearheaded the creation of employment and protection of financial assets. It has been paramount saving hub and investment channel (CBK, 2020).

5.4 Policy Recommendation

The researcher recommends the policy regulation that enhance the growth of the bank to enhance the bank size. The banks are paramount in the monitoring the economic growth of the country. The research is the protect and safeguard money. The paramount investments opportunities have been reinforced in the discharge of social mandate and promotion of the standard of living. The rules and regulations that protect the banks should be reinforced and initiated to enhance financial sustainability and earning quality.

The banking industry must implement the debts level that they can withstand in the longevity. The credit risk must be maintained and monitor to avert losses and increases the productivity of the commercial banks. The earning quality must be monitored to promote the reputation, enhance growth, and increase the bank market base. The economic prosperity and development of a progressive country is determined by the market base of a country. The technological advancement should be incorporated in the operation of the banks.

The management efficiency is crucial in the earning quality. The regression and descriptive analysis postulated the importance of management in the earning quality. The corporate governance must promote prospective policies that promote banks' growth. The management inefficiency should be eliminated, and innovative minds put in place to drive the banking industry forward. Management efficiency regulation must be promoted to increase the productivity and earning quality.

This research add knowledge on the existing policies and draft strategies that enhance the growth. The research solves the banking problems and creates a blueprint for transformation in the banking industry. The banking sector is indispensable and salient in the futuristic development of any nation. The banks accelerate growth, industrialization, proliferation, and dynamic transformation. In a nutshell, the leverage has a significant effect on the earning quality.

5.5 Limitation of the study

The research concentrated on the commercial banks in Kenya and did not look at other sectors. The crucial economic development is not tied to one sector. Furthermore, the research focused on the four key determinants in the study. There is need for the study scalable and digital led impacts on the commercial banks to shed more lights. The research involved the collection of data spanning from a period of five years.

The research optimized historical data sourced from commercial banks and central banks of Kenya. The historical data was imperative in obtaining the past pattern of events in the commercial banks. However, it may not reflect the current position of the banks. The structures, policies and technology have changed and has substantial impact on the commercial banks. The commercial banks are the drivers of the economic growth hence there is need for accurate findings.

5.6 Areas of further research

This research advocate for further assessment of the effect of management efficient on the earning quality of commercial banks in Kenya. The investigation will build a useful and paramount finding on the role of corporate governance in enhancing the accrual earning. The study will fill the gap that has been existing between the audits. The aspiration on the research topic should be to promote accountability and transparency in the management of banks.

The research should do assessment on the impact of bank size on the earning quality. The determinants of bank size such as technological advancement must be put into consideration. Furthermore, the research should scrutinize integral part of bank size and find the association and correlation with earning quality. This will be a major milestone in establishing strategic pillars of earning quality.

The research stipulates the need for the research on the earning smoothing and the growth of commercial banks. The smoothing has been one of the key emerging issues in the performance of banking sectors. The managers have been declaring profit throughout and evaluating critically it has been boosted by smoothened earnings. The vibrant banks need radical measures that enhance service delivery in the banking platform.

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APPENDICES

APPENDIX I: LIST OF COMMERCIAL BANKS

BANKS	2016	2017	2018	2019	2020
ABC Bank					
African Banking Corporation					
African Development Bank Group					
Afrika Investment Bank					
Bank of Africa Kenya Ltd					
Bank of Baroda (Kenya) Ltd.					
Central Bank of Kenya					
CFC Stanbic Bank Limited					
Chase Bank					
Citibank N A					
Commercial Bank of Africa					
Consolidated Bank					
Co-operative Bank					
Development Bank of Kenya Ltd					
Dry Associates Limited					
Dubai Bank Kenya Ltd					
Dyer & Blair Investment Bank					
Equatorial Commercial Bank Limited					
Equatorial Investment Bank					
Equity Bank					
Faida Investment Bank – FIB					
Fidelity Bank					
Fina Bank					
Giro Commercial Bank Ltd					
Guardian Bank Ltd.					
Housing Finance					
Imperial Bank Limited					
Investments & Mortgages Bank Limited – I&M Bank					
KCB Bank					
Kenya Post Office Savings Bank					
K-Rep Bank					
National Bank					
NIC Bank					
Oriental Commercial Bank Ltd.					
Paramount Bank					
Prime Bank					
Standard Chartered					
Standard Investment Bank					

Sterling Investment Bank					
Suntra Investment Bank Ltd					
The Co-operative Bank					
UBA Kenya Bank Ltd					

APPENDIX II: EARNINGS QUALITY

2016	2017	2018	2019	2020
0.030	0.038	0.062	0.040	0.037
0.028	0.038	0.055	0.040	0.450
0.022	0.013	0.032	0.038	0.039
0.031	0.028	0.030	0.029	0.031
0.024	0.021	0.031	0.312	0.038
0.024	0.028	0.027	0.028	0.051
0.027	0.029	0.028	0.029	0.030
0.025	0.037	0.029	0.030	0.037
0.036	0.026	0.030	0.036	0.043
0.024	0.029	0.038	0.024	0.007
0.028	0.035	0.035	0.031	0.035
0.027	0.037	0.040	0.022	0.027
0.023	0.024	0.032	0.038	0.028
0.037	0.038	0.025	0.055	0.043
0.024	0.027	0.033	0.041	0.074
0.035	0.036	0.030	0.032	0.073
0.048	0.036	0.040	0.023	0.034
0.048	0.021	0.051	0.025	0.037
0.035	0.082	0.040	0.022	0.037
0.024	0.017	0.025	0.023	0.030
0.023	0.025	0.021	0.041	0.050
0.023	0.026	0.027	0.057	0.050
0.021	0.055	0.028	0.033	0.024
0.012	0.032	0.028	0.022	0.053
0.038	0.073	0.058	0.027	0.040
0.025	0.0362	0.039	0.023	0.075
0.051	0.025	0.073	0.052	0.077
0036	0.240	0.0767	0.039	0.045
0.072	0.028	0.076	0.074	0.051
0.037	0.072	0.025	0.077	0.077
0.190	0.022	0.025	0.099	0.027
0.023	0.083	0.066	0.022	0.066
0.008	0.023	0.023	0.027	0.033
0.067	0.033	0.084	0.081	0.086
0.011	0.021	0.025	0.031	0.029
0.049	0.056	0.056	0.048	0.045
0.036	0.015	0.064	0.049	0.064
0.032	0.031	0.028	0.038	0.031
0.045	0.041	0.045	0.040	0.053
0.042	0.041	0.046	0.043	0.040
0.044	0.030	0.038	0.033	0.075
0.041	0.033	0.034	0.033	0.085

APPENDIX III: DEGREE OF FINANCIAL LEVERAGE

2016	2017	2018	2019	2020
1.501	1.673	1.162	1.250	1.333
2.370	1.781	1.755	1.403	2.114
1.872	1.981	1.801	1.749	2.284
2.143	1.943	1.891	1.670	2.844
4.433	3.559	3.395	2.011	2.344
1.465	1.650	1.500	1.400	1.765
7.661	2.511	4.424	2.511	2.111
2.781	2.071	1.838	1.726	1.900
1.502	1.589	1.307	1.381	1.399
1.380	1.350	1.299	1.354	1.389
1.711	2.011	1.999	1.667	1.789
1.233	1.108	1.110	1.380	1.792
2.146	2.203	1.990	1.699	2.441
2.274	2.301	1.999	1.255	2.445
1.890	1.768	2.201	1.685	2.521
1.473	1.950	2.093	1.991	1.830
1.890	1.707	1.860	1.673	1.985
2.380	1.790	1.990	1.887	1.840
1.723	1.881	1.820	1.789	1.840
1.915	1.997	1.990	1.890	1.962
2.068	1.776	1.839	1.779	1.899
1.999	1.754	1.899	2.221	1.377
2.141	2.471	2.330	2.001	1.992
1.768	1.890	2.021	1.873	2.044
2.512	1.997	2.789	2.630	1.994
1.967	2.781	2.812	2.099	2.730
2.141	1.891	1.983	2.000	1.997
2.163	1.630	1.530	2.899	2.771
1.768	1.891	2.973	2.274	1.673
2.512	2.673	1.877	1.891	1.972
1.789	1.882	1.877	2.274	1.972
1.967	1.537	1.686	1.891	2.289
1.466	1.699	1.697	1.732	1.897
1.503	1.789	1.831	1.679	1.819
1.870	1.969	1.932	1.383	1.493
1.671	1.996	1.873	1.881	1.823
1.891	1.969	1.991	1.772	1.677
1.762	1.778	1.831	1.781	1.893
1.891	1.789	1.831	1.761	1.678
1.772	1.623	1.772	1.689	1.531
1.624	1.560	1.611	1.649	1.671
1.523	1.581	1.581	1.679	1.891

APPENDIX IV: BANK SIZE

2016	2017	2018	2019	2020
18.88	18.94	18.77	19.04	19.12
17.58	17.61	17.68	17.70	17.89
17.21	17.31	17.45	17.50	17.60
16.20	16.22	16.79	17.79	17.89
18.72	18.55	18.78	18.80	18.95
17.72	17.75	17.80	17.88	17.90
17.80	17.81	17.87	17.90	18.98
17.99	17.99	18.23	18.25	18.30
18.23	18.24	18.45	18.48	18.54
18.43	18.46	18.48	18.49	18.56
17.54	17.81	17.99	18.03	18.08
16.54	16.57	16.59	18.04	18.10
19.21	19.33	19.45	19.92	20.00
17.93	17.99	18.21	18.24	18.55
18.93	18.97	18.90	18.95	19.45
18.40	18.55	18.60	18.69	18.75
18.52	18.55	18.64	18.70	18.77
18.55	18.49	18.56	18.58	18.64
18.78	18.79	18.97	18.91	19.23
18.30	18.50	18.79	18.79	18.87
17.79	17.76	17.80	17.86	17.85
19.20	19.30	19.45	19.49	19.50
17.89	17.90	17.93	17.97	18.03
16.72	16.89	16.83	17.00	17.04
18.80	18.89	18.92	18.93	18.99
18.12	18.13	18.23	18.43	18.45
18.88	18.89	18.95	18.99	20.01
16.53	16.60	16.65	16.67	16.90
18.88	18.90	18.95	18.95	18.99
17.28	17.30	17.38	17.55	17.87
18.23	18.30	18.34	18.45	18.55
16.27	16.30	16.38	18.40	18.41
18.99	19.02	19.10	19.11	19.12
17.99	18.12	18.22	18.23	18.45
18.34	18.33	18.38	18.45	18.73
17.99	18.30	18.31	18.31	18.40
18.44	18.32	18.44	18.50	18.53
18.34	18.45	18.31	18.61	18.72
18.72	18.52	18.77	18.78	18.62
18.34	18.22	18.33	18.27	18.66
18.22	18.65	18.66	18.65	18.76
18.41	18.43	18.11	18.40	18.45

APPENDIX V: MANAGEMENT EFFICIENT

2016	2017	2018	2019	2020
1.02	0.68	0.89	1.02	1.03
1.54	1.69	1.23	1.70	1.85
1.99	1.65	1.98	0.98	1.09
1.62	1.60	1.01	1.53	1.78
1.43	1.24	1.31	1.06	1.62
1.40	1.82	1.60	0.54	1.53
1.48	0.70	0.75	1.33	1.02
1.88	1.53	1.25	0.24	0.25
0.99	0.88	0.51	1.38	1.39
1.38	3.45	1.99	2.25	2.78
1.27	2.89	1.72	1.67	1.78
1.90	1.74	2.73	4.99	4.50
2.70	1.88	1.69	1.50	1.67
2.22	5.24	1.34	1.23	1.81
1.99	2.53	1.21	1.98	1.73
1.65	1.67	2.51	1.27	1.46
2.35	2.05	0.99	1.04	1.53
1.24	3.42	2.00	0.98	1.09
1.95	2.88	1.21	0.37	1.62
1.89	1.92	0.90	2.95	1.90
1.88	1.87	2.53	2.70	1.78
1.87	1.99	2.67	2.54	1.77
0.77	1.77	0.58	0.68	1.69
2.10	2.13	0.67	0.77	1.74
1.76	1.73	1.99	1.98	1.98
3.22	3.23	2.11	2.12	1.99
1.89	1.90	3.24	3.22	2.99
3.12	3.13	2.69	2.79	2.87
4.20	3.24	4.00	4.00	4.01
4.22	4.25	4.23	4.32	4.10
2.89	2.90	1.56	1.89	1.90
1.79	1.80	1.77	1.77	1.86
1.73	1.78	0.52	2.04	1.53
0.70	0.99	1.66	1.24	1.72
2.22	2.44	2.53	2.38	2.32
2.05	2.13	1.86	2.00	1.89
1.90	2.13	1.78	1.64	1.79
2.12	1.98	1.56	1.69	2.23
1.91	2.20	1.43	1.79	2.34
1.89	1.89	1.50	2.00	1.89
1.99	1.98	2.01	2.22	2.33

APPENDIX VI: CREDIT RISK MANAGEMENT

2016	2017	2018	2019	2020
0.053	0.059	0.063	0.067	0.052
0.067	0.069	0.070	0.073	0.077
0.020	0.025	0.023	0.032	0.089
0.031	0.035	0.040	0.063	0.034
0.910	0.083	0.081	0.087	0.090
0.068	0.062	0.068	0.077	0.069
0.435	0.380	0.079	0.69	0.072
0.867	0.532	0.068	0.079	0.078
0.112	0.132	0.099	0.074	0.562
0.087	0.084	0.232	0.0789	0.074
0.064	0.067	0.069	0.052	0.053
0.043	0.044	0.048	0.123	0.089
0.005	0.083	0.090	0.060	0.077
0.027	0.045	0.050	0.037	0.030
0.040	0.086	0.082	0.047	0.036
0.030	0.035	0.031	0.230	0.047
0.036	0.035	0.032	0.530	0.021
0.187	0.189	0.380	0.530	0.544
0.480	0.052	0.790	0.795	0.084
0.930	0.890	0.052	0.048	0.0732
0.033	0.042	0.072	0.075	0.090
0.042	0.036	0.072	0.089	0.089
0.039	0.025	0.062	0.028	0.082
0.085	0.028	0.023	0.079	0.064
0.084	0.092	0.069	0.089	0.070
0.086	0.068	0.079	0.069	.069
0.087	0.078	0.080	0.069	0.089
0.067	0.069	0.080	0.069	0.078
0.089	0.079	0.095	0.0891	0.076
0.094	0.012	0.273	0.069	0.077
0.045	0.076	0.078	0.081	0.082
0.046	0.050	0.052	0.030	0.053
0.041	0.059	0.050	0.060	0.086
0.035	0.034	0.038	0.083	0.086
0.036	0.042	0.350	0.474	0.082
0.034	0.036	0.351	0.055	0.089
0.087	0.094	0.080	0.474	0.085
0.089	0.0895	0.075	0.055	0.099
0.045	0.092	0.072	0.056	0.084
0.011	0.089	0.072	0.055	0.052
0.123	0.023	0.077	0.012	0.068
0.056	0.961	0.067	0.543	0.567