CAPITAL STRUCTURE AND FINANCIAL PERFORMANCE OF ISLAMIC BANKS IN KENYA.

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JULY, 2018
DECLARATION

This research project is my original work and has not been presented for a degree or other
award in any other university. No part of this research project should be reproduced without
authority of the author or / and Kenyatta University.

Signed: 

Date: 

AHMED SHARIFF SALIM

D53/MSA/PT/33160/2014

This research project has been submitted for examination with my approval as the
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Signed: 

Date: 

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Kenyatta University.
DEDICATION

This is for you, mom and to my special friend queen, who kept me working when I wanted to give up.
ACKNOWLEDGEMENTS

I give all tributes to the exalted Allah (S.W) for the reward of life, good well-being and prospect to realize this program. I also thank the school of business for giving me this opportunity to attain an MBA. I give copious appreciativeness to my supervisor; Mr. Samson Kaplelach for his patience and great guidance throughout the period that I have carried out this project. To my exceptional kinfolk for their material and moral support as well as their prayers special thanks also to my associates for their backing and inspiration. May Almighty God; abundantly reward you all.
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<td>Islamic Bank</td>
</tr>
<tr>
<td>CBK</td>
<td>Central Bank of Kenya</td>
</tr>
<tr>
<td>OIC</td>
<td>Organization of Islamic Conference</td>
</tr>
<tr>
<td>PSE</td>
<td>Palestinian Security Exchange</td>
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OPERATIONAL DEFINITION OF TERMS

Capital Structure

It is the way a firm finances its sources of funds for investment mostly through assets by use of debt and equity combination (Saad, 2010). And according to Ahmadpour and Yahyazadehfar, (2010) Capital Structure is combination of debt and equity that makes up the sources of corporate assets.

Islamic Banks

Muhammad, in his book financial institutions of contemporary people (2000: 62, 63) defines that Islamic Banking is: "Financial institutions are businesses primarily providing financing and other services, the traffic and circulation of cash payments adjusted with the implementation of Islamic law".

Conventional Bank

According to the Black’s Law Dictionary a bank is defined as “A quasi-public institution, for the custody and loan of money, the exchange and transmission of the same by means of bills and drafts, and the issuance of its own promissory notes, payable to bearer, as currency, or for the exercise of one or more of these functions”

Shariah

Atlantic Council (Rafik Hariri center for the Middle East) defines it as
It is the body of Islamic rules and teachings that governs Muslims’ relationships with their families, society, and nation. Sharia law derives from eleven Islamic references, primarily the Holy Quran, the holy Muslim scripture revealed to the Prophet Mohamed, and the prophetic tradition, i.e., the recorded words and actions of Prophet Muhammad that mainly illustrate and explain the Quran.

**Short term debt**

Items that will be used, liquidated, mature or paid off within one year (Guin (2011)).

**Financial Performance**

It denotes to a firm’s capacity to breed new resources from day to day operations over a given period of time (Bora, 2008). It involves improving owners’ wealth and revenue creation which are amongst the chief intentions of a firm (Pandey, 2005).
ABSTRACT
The banking sector primarily differing from the other section of the market vast quandary for administration and financiers comparable is whether or not a most favorable capital structure exists and the way numerous capital structure choices each immediate and lasting persuade business level of performance. The choice on which capital structure to select is among the foremost important and decisive choices within the banks as a result they have an influence on the financial performance of the banks. Totally different writers have different view over the weight of capital structure on the financial performance of commercial banks. The meager studies during this field, on effects of capital structure generated a data gap that galvanized this study. This project aspired to review effect of capital structure on Islamic banks’ (IBs) financial performance as from 2011-2015 because during this era of study, Kenya encountered political anxiety, resulting in insecurity within the stock exchange and the general elections held in 2013 were the first under the Constitution of Kenya 2010 and ushered in a major transformative devolved governance system of 47 county governments. Since then, the government has been putting in place various legal, regulatory frameworks and the relevant supporting institutions aimed at implementing the constitutional provisions for successful implementation of devolution. As tenderfeet to the souks, IBs face a trade-off. They will either create use of high capital proportions that amplify the reliableness and security of the bank and worsen the specified take by investors or depend upon deposits and Islamic bonds that are deemed as economical sources of funds because of their tax recompense. In recent times in Kenya, there has been a big swell within the variety of recent creativity to expand and progress the concept of Islamic financing. Commercial banks are reformatting their growth strategies to focus more on the speedy growing Islamic banking business as they aim bigger client numbers and more revenues. Although still looked upon as a budding notion in Kenya’s banking business, shariah-compliant products have gradually achieved recognition over the last diminutive years and banks’ top cream now have their arsenals ready to fight for a piece of the pie. There are forty two commissioned commercial banks in Kenya. Among them, only two, the Gulf African bank and first Community bank are fully-fledged Islamic banks. Using secondary panel data contained within the yearly reports of the 2 Islamic banks in Kenya covering the years 2011 to 2015 the study used return on equity (ROE) and return on assets (ROA) as dependent variable and 5 capital structure measures (including Firm’s age, asset tangibility, Growth opportunities, financial leverage and Size of the firm) as experimental variable. This study employed an explanatory non-experimental research design and the gathered facts were then entered into the Statistical Program for Social Sciences (SPSS) and multiple regression analysis method was used to analyze. Pearson's correlation coefficient was determined and Kolmogorov-Smirnov goodness of fit test was done. The findings showed that the growth opportunities and size of the firm have an affirmative and large impact on financial performance of the Islamic banks of Kenya, whereas the age of the firm and the asset tangibility encompasses a negative and weighty impact on financial performance of the Islamic banks. Hence, this study complete that size of the Islamic banks and the growth opportunities of Islamic banks in Kenya enhance financial performance, whereas the age of the firm and conjointly the asset tangibility reduces financial performance of Islamic banks while the financial leverage of the Islamic banks has no impact to the financial performance of Islamic banks in Kenya.
CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Since 1900s Islamic economists and scholars’ commenced analysis of conventional banks in Muslim countries and a numeral of savings institutes were well-known in the 1960s. In 1975 Dubai Islamic Bank commenced operations and it was among the first Islamic banks to be established. From 1980s the Islamic banks around the globe started to increase more in numbers as in 2008, the number of Islamic commercial institutes across over 50 countries had exceeded 300. As the awareness increases regarding Islamic banks services both Muslims and non-Muslims started opting for Islamic banking facilities thus this fuelled the growth of the Islamic banks. (Hassan & Lewis, 2009)

Islamic banks may be defined differently by different Islamic jurist but according to Organization of Islamic Conference (OIC) it delineates it as “a monetary institute whose decrees, guidelines and dealings explicitly explains its binder to the Doctrines of Islamic Shariah and to the prohibition of the receiving and recompense of interest on any of its operations”. Tayyebi (2008) describes Islamic Finance as “any Finance that is compliant with the principles of Islamic Law”. for the past five years Islamic banks has attracted a lot of attention and it is among the fastest growing segments of the financial services market with annual growth rate averaging 15 percent(Gachuhi,2016). He continues saying that in spite of all this; still there are a lot of question marks on understanding the system that
prohibits the payment and receipts of interest. In Islam cash is not taken as a producing asset in plus of itself, Islam as a whole put much consideration on the virtuous, decent, communal, and religious factors to promote equivalence and impartiality in the society. Although Islamic banking emphases on its economic aspects, the system is fully understood only in the framework of Islamic attitudes toward ethics, social, wealth distribution, pecuniary integrity and the starring role of the regime. In Islam there is a code governing the contracts underlying the banking system. (Iqbal & Molyneux, 2005)

Saad (2010) explains that if by chance that anyone wants to borrow or lend funds, according to Islamic perception the sources have to be fitting in a manner that is permitted by Islamic shariah. The amount requisite in financing the activity must be screened and a clear way of how the money is to be repaid must be aligned with the laws of Islamic financing. With every house there are rules prevailing the operations the same applies with Islamic banks. They also periodically carry out an analysis of their performance for the concern of the executive, the shareholders, government (Bank of Kenya) so as to plan and determine its business policy for the anticipatable future. Islamic finance has recently been growing and has earned a positive responsiveness in Kenya. Its elasticity has placed the shariah compliant monetary system as a robust substitute to conformist banking system. In the dominion of banking, capital structure is among the key topics amongst specialists in finance. Saad (2010) maintained that in finance capital structure explains a fashion in which a business finances its assets across the amalgam of hybrid securities, equity and debt.
The capital structure and ROE relationship is undeniably significant to all firms, since banks are delicate to alterations in financial leverage the capital structure decision become an important pillar and that is why the banks’ capital structure is greatly regulated. Capital arrangement choices aren’t only essential for administrators and regulators, but different stakeholders are keen to different decisions taken by the banks for their own interest. For instance equity holders are interested because it determines the rate of return and safety of the investment in the bank. A bank with high leverage is more risky but in other hand it offers greater returns to owners. As a result, the capital structure choice enacts a risk-return trade-off for the bank. (Pandey, 2009)

Generally the banks in order to capitalize on their return on capital and satisfy of their financiers they are a requisite to retain a lowest capital ratio by governing authorities and ranking agencies (CBK Prudential Guidelines, 2013). Conversely, these banks have the trend to exchange capital with liability, which is inconsistency to Modigliani and Miller’s (1958) irrelevance theory. The faith that banks can surge their results by replacing investment with liability is not the outcome of disregarding the risk effect of leverage. Memmel and Raupach (2007) stated that desirability of higher leverage for banks is required.

One of the traits of Islamic banks (IBs) is that they are all equity institutions and Investment deposits feature is that their wealth worth and degree of yield do not have a guarantee. In most cases the depositors in IBs are the shareholders, so they end up earning dividends when the banks make profits. Despite the argument that the deposits are more of like equity, banks
practicing IB diverge from its optimal form in a few different ways. One is that all deposits (including investments) are guaranteed to the extent that laws and regulations are formally formed on implied understanding between the banks experts and the public. (Gachuhi, 2016)

Zaher and Hassan(2001), statuses that Current account holders are treated as creditors in Islamic banks. Besides, information unevenness and risk abhorrence behavior of financiers, currently a fixed claim liability exists on IBs’ statement of financial positions. Thus, IBs ought to maneuver under capital sufficiency regulations, but in actuality they had better be functioning as having an equity built capital structure. Controllers in Western countries will claim that IBs ought to transmit more wealth, as Islamic banking is new and for the reason that IBs’ assets are frequently of a longer period and illiquid.

Being as tenderfoots to the souk IBs are facing a trade-off. They have the option of either using greater capital so as to increases trustworthiness and welfare of the bank and lower the vital profit from depositors and shareholders. This will cause a higher productivity, or in other hand they can be contingent on credits and Islamic bonds which are typically measured low-priced bases of resources owing to their tax deductibility, resultant in the higher performance. (Halkano, 2009)

In the economy, banks and monetary organizations play a vibrant part in providing economic stability as a result of their monetary policy. Abu-Rub (2012) examined the influence of capital structure on non-monetary company's execution. He used panel data procedure on a model of 28 registered corporations on the Palestinian Securities Exchange
(PSE) from 2006 - 2010. The outcome exhibited that business’s capital structure impacted the company’s execution in bookkeeping and market’s measures.

The use of financial leverage directly affects capital structure of a firm. The association between earnings before interest and taxes together with earnings before tax it is all what financial leverage is all about. The more debt a business has in its assets structure, the grander its financial risk. Thus the degree of this risk and the related potion of returns are key contributors to the appraisal process; a company must approximate the influence of elective capital structures on these aspects and eventually on significance cause of opting for the best capital structure (Makau, 2006).

Chowdhury and Chowdhury (2010) noted that banks old-style approach of attainment of resources at a stumpy price and the range amid getting monies and lending out credits and advances has reduced thus yielding low profits this forced the banks into looking for new paths so as to increase their revenues. According to Chowdhury, risks can be diversified by increasing the fee based income. The capital structure and financial performance are relatively vital to banks in shaping the financial patterns. For instance, in a study by Omet and Nobanee (2001) noticed that smaller firms when compared to large firms held a low percentage of debt in their capital structure. Such discoveries are useful to the banks in ruling out which financial patterns they can adopt in the brief and the everlasting. This helps in shaping their firms accordingly.
Kenya is the chief country in introducing Islamic banking in the Eastern and Central African region. Its progress echoes a drift international where it has been emergent than banking assets as a whole. An uprising is winning place in the finance and banking sector; the relentless development of Islamic banking in the nation but still politics and social inter-religious relations govern all the captions and not constantly for the right motives. When the concept of Islamic banking was first familiarized in Kenya about a decade ago, it was embraced by a lesser Muslim cream of the crop but as of now the gigantic common of the regulars is non-Muslim. For example in the year 2015, the National Bank of Kenya released 25,000 accounts in its Islamic banking window, National Amanah, almost 19,000 of which are held by non-Muslims (Gachuhi, 2016).

1.1.1 Capital Structure

Banks are incorporated entity, and as the rule of the thumb must be backed by a certain amount of principal. One of the ways that the banks secure capital is by marketing capital stock to investors and as the banking rules and regulation is that each bank must uphold a tiniest amount of capital. The money that the owners pay for the capital stock it becomes the working capital of the bank, (according to CBK prudential guidelines,2013) Business banks tasks in Kenya are controlled by CBK which characterizes the environment in which these banks ought to work. It additionally sets the different capital necessities that any business bank ought to work by setting up least capital prerequisites. CBK Prudential Guidelines (2013) part 3 states that capital necessities for a particular establishment may rise or lessen relying on its risk profile.
Capital structure of any foundation ought to along these lines be very much figured out how to guarantee that the firm stays in task and it's ready to back its undertakings. Accordingly, the way a bank joins its obligation and value, will characterize its execution as verified by (Ross et al., 2009). It is broadly accepted in the banking literature that equity is an exorbitant type of back for banks and other budgetary establishments (Flannery and Rangan, 2008). This proposes banks ought to limit the measure of capital they utilize, and if there is an administrative least, this ought to tie. By and by, this isn't the situation (Flannery and Rangan, 2008).

Awunyo and Badu (2012) mentioned an objective fact that the normal capital structure of the recorded Banks on the Ghana Stock trade was 87% from 2000 to 2010 suggesting the banks recorded on the Exchange are exceptionally adapted. The abnormal state of outfitting watched sum the banks can be credited to their over reliance on here and now obligation thus generally high Bank of Ghana Lending rate and low level of security showcase exercises

The similitudes between the banks and non-monetary related firms' capital structure might be more prominent than beforehand thought, as supported by (Gropp and Heider, 2009). They watched that most determinants of capital structure in different firms likewise apply to saves money with special case of those banks which are near least capital prerequisites. They also observed that banks back their announcement of money related position development completely with non-deposit liabilities meaning structure of banks add up to liabilities has moved far from deposits. It is in this way, hard to express the ideal capital
structure of a bank since they appear to require stable capital structures at stages that are specific to every discrete bank. In this manner in a dynamic structure, banks' objective use is time invariant and Bank particular (Gropp et al., 2009).

1.1.2 Financial Performance

Different shareholders may give different definition of a business’s financial performance, in the sight of the investor, a financial performance is dignified by how healthier the investor is at the finale of a period, than how he was at the commencement. According to Berger and Patti (2002) this can be obtained using proportions derived from financial reports or by statistics on stock market prices. Financial performance of a bank is defined as its ability to produce supportable productivity, (European Central Bank (ECB), 2010) Key drivers of measuring bank performances are earnings, efficiency, risk taking and leverage, (ECB, 2010). Firstly, a bank must be able to generate earnings to remain in operation, secondly, it should be able to adjust its earnings to overcome the various risks involved such as credit and make profits, thirdly risk it should be efficient meaning it should be able to generate revenue from the given assets and finally it should be able to improve its results through the way it functions.

The main measure of financial performance is through ratio analysis which has been identified as convenient and efficient method of assessment since it combines information from financial statements and comes up with numbers that are more easily interpreted, (Burckhardt, 2013). Abumin (2009) expressed that the significance of bank gain may be gauged at the microeconomic level and macroeconomic level. At the micro-economic level, the result's essential for the competition and it's the supply of funds. At the macroeconomic level, a strong and productive banking sector can withstand antagonistic stuns and adds to
the quality of the saving money and budgetary framework. The profits of the bank area are a crucial unit of supply of capital especially if they're reinvested within the business.

Studies coping with in-house determinants use variables like capital, size, expenses management and risk management, human resource and bank originality. External determinants of bank monetary performance embody factors like interest rates, inflation and alternating yield, and variables that denote market features (Alam et al., 2011). Revenue is the final objective of banks. All the ways calculated therefrom are preordained to comprehend this ostentatious objective. Nonetheless, this doesn't mean that banks don't have any alternative goals. Banks may even have further socioeconomic goals. Though, the intent of this study is expounded to the financial performance of the Islamic banks; to measure the financial performance of business banks there are kind of ratios used of which (ROA) return on asset, (ROE) return on Equity and net Interest Margin are the foremost ones (Murthy & Sree, 2003; Alexandru et al., 2008)

1.1.3 Capital Structure and financial performance

One necessary deduction is that the structure of a firm’s capital has insinuations for its maneuvers and effects on its financial performance (Berger and Bonaccorsi, 2006). An excellent perplexity for administration and financiers alike is whether or not there subsists a best capital structure. The target of all finance selections is wealth maximization and also the fast approach of assessing the excellence of any funding call is to look at the result of such a choice on the firm’s performance (Salazar et al, 2012).
Abdulrahman and Al-Sabaawee (2011) their study tried to assess the performance of IBs over the usage of complex viability, stability and profitability of business. He resolved that IBs if they want to attain the socioeconomic objectives and along their rudiments base, it’s indispensable to have a part of pronounced judgment making and financial strategies and upcoming plans, and strengthening the position of these banks in the societies working in it, as well as the use of financial instruments provided by the financial analysis in order to reach the goals that are supposed to be achieved. While Sidqqui and Shoaib, (2011) established in their study “Measuring performance through capital structure in Pakistan” that size of the bank plays a vital role in deciding the profitableness of the bank using ROE as profit measure. Additionally, Tobin’s Q model was conjointly utilized in the study to measure banks profit and performance and located direct and positive relation with the leverage ratio, size of the banks and Investments by banks in assets.

The capital structure and financial performance are also important to banks in determining the financial patterns. For instance, in a study by Omet and Nobanee (2001) noticed that large firms held a bigger share of liability in their capital structure, compared to smaller firms. Sathye (2005) noticed that denationalized banks have achieved well than fully public sector banks and this was attributed to banks performance and efficiency shown. Bhaumik and Dimova (2004) reports that factors such as direct investments, progress in assets, direct credit etc. shakes the profitability and efficiency of the banks.

However, there is the other side of the coin a negative relation of debt and firm profitability some studies have shown that for example Kaumbuthu (2011) applied a study on capital
structure and ROE for manufacturing and associated sectors within the Nairobi Securities Exchange as from 2004 to 2008. Capital structure was proxies by debt equity ratio whereas performance centered on ROE. Multivariate analysis was applied and an adverse relationship between debt equity ratio and ROE was obtained. One segment of the businesses listed in Nairobi Securities Exchange was attended and paid devotion to simply one facet of funding choices. The outcomes hence might not be sweeping to the opposite sectors. In an endeavor to corroborate MM theory in African country, Maina and Kondongo (2013) examined the impact of debt-equity ratio performance of companies listed at the NSE. The sample was a poll of all firms registered at the NSE from 2002 to 2011. A major deleterious relationship between determinant of performance and capital structure was recorded.

A polish study by Hammes (2003) he made a comparison of Hungarian and Polish companies to a enormous model of companies in manufacturing countries, by using panel data analysis to explore the liaison among diverse bases of debt to be precise, trade credits and bank loans and companies’ performance measured by profitability. His outcomes revealed a deleterious outcome for most countries and that the sort of debt is not of major prominence, what substances is debt in overall

1.1.4 Islamic Banks in Kenya

According to Kenya Commercial Bank (2013) credit rating report, Kenya Commercial Bank, group is preponderantly backed over by client shareholders equity, deposits and to a
partly indebtedness. If registered, the cluster will rise further capital through the stock market. In Kenya, Islamic banks don't seem to be clearly well-defined within the Banking Act. Out of the 43 commercial banks, 2 banks (Dubai Bank and Imperial Bank) have since been closed and put under management of the Central Bank of Kenya. The sector is controlled by the Central Bank of Kenya (CBK) as authorized by the Banking Act (Central Bank of Kenya, 2014). Among them, only two, the Gulf African bank and First Community bank are well-developed Islamic banks. The conventional commercial banks have set up Islamic windows offering Islamic products and services (Gachuhi, 2016). He continues by saying a small number of Kenya’s giant banks now have “openings” for Islamic banking. These are managed by cream of the crop well considered in their knowledge of Shariah law and a committee of Islamic scholars who are autonomous from the banks’ administration. Their understanding of the law is mandatory on the banks and its clienteles

Commercial banks generate operating profits primarily from two key areas net interest income and non-interest income. Net interest income emanates from bank activities involving sourcing of funding (liquidity) at low rates and deploying (lending) the funds at higher rates, the margin there-from being the profit. Non-interest income (mainly fees and commissions) are revenue streams from services rendered by the bank, excluding interest income. The performance of the Kenyan banking sector has improved in recent years. The arena has emerged from a high non-performing loans atmosphere within the 80’s, 90’s and early 2000’s a period when many banks collapsed due to the high non-performing loans. The high non-performing loans environment was partially due to weak credit risk management,
weak company governance and non performing government connected debt (Central Bank of Republic of Kenya, 2013).

For this study will use only the two fully fledged banks because the others are conventional and previous studies have covered it. For IBs, Capital structure isn't identical: Islamic banks are governed by shariah law. Shariah law proscribes, among various stuffs, recompense and acceptance of riba (interest). This infers that IBs can’t earn or pay interests on their monetary instruments. The banks are left to drum up and employ treasuries using Shariah-compliant mechanisms or conventions that don't seem to be utilized by their typical counterparts (Harzi, 2009) what is more, per the shariah law rules; investors portion their profits and losses with Islamic banks. The Mudaraba convention transforms a partnership tie between the bank and its investors. This lowers the leverage in return induce bank to realize a better profit. The foundations of MM theory are impacted as well as the predictions of the standard college that are supported by debt finance, can't be universal to incorporate Islamic banks. In typical banks the price of capital is value of debt and equity deposit while in Islamic banks the price of capital is interchanged by profit and loss sharing by savers and shareholders’. Typical banks either borrow or issue common stocks to finance their investments, whereas Islamic banks back their investments using primarily equity funding and customers’ bank account (Mayhem, 2017)
1.2 Statement of the problem

A study by Chisti et al (2013) states that call creating has emerged in concert of the hardest chores because it elects the providence of each firm. They believe that the side of capital structure decision is significant, since the financial Performance of an enterprise is directly plagued by such call. Hence, correct care and a spotlight ought to lean whereas creating the capital structure call (Chisti et al, 2013). Sufian (2009), states that the banking sector is the pillar of China’s economic system and it plays a very main financial intercession role within the country’s economy. He additional explains that the health of banks is important to the wellbeing of the overall economy at large. This position is applicable within the Kenyan context.

Succeeding the effort of Modigliani and Miller (1958 and 1963), more exploration are done in business finance to express the stimulus of a company’s select of capital structure on performance. The firms work diligently when shaping their finance so as to have a good bearing on performance as achievement in the trade is decisive to the worth of the firm and its existence. The capital structure of banks is, in any case, still a generally under-investigated region in the banking literature. At present, there remains not any unmistakable comprehension on in what way banks pick their capital structure and what dynamics impact their corporate funding conduct. The capital structure of banks is to a great extent dictated by the benefit side of the statement of financial positions, (Diamond and Rajan, 2000).

Studies within the last twenty years have exposed that business banks in sub-Saharan geographical region are additional money-making than the remainder of the globe with a
median ROA of 2% (Flamini et al., 2009). Kiprotich (2012) studied the effect of financial structure on the performance of commercial banks in Kenya. He found out that commercial banks prefer short term leverage as their source of capital. Halkano (2012) paralleled the performance of conventional vs. Islamic banks in Kenya. They found that conventional banks performed better than Islamic banks. They also learned that Islamic banks were more liquid than conventional banks but had more inherent risks to investors.

Ongore (2011) studied financial performance of the Kenyan banks and found that the sector was quite profitable. Among the stimuli that influenced the financial performance of the firms lied with various choices on financial structures such as ownership identity. Oloo (2011) also noticed that regardless of the worthy general financial performance of banks in Kenya, around are a couple of banks which were pronouncing losses and faced bailouts. Of the banks that were announcing losses, IBs were observed to be amongst them. This makes IBs appear not profitable in this lucrative undertaking. Islamic banks are known to have a different financial structure from other conventional banks that are recording profits in the banking sector. This study therefore intended to address the following research enquiry: What is the effect of capital structure on the financial performance of Islamic banks in Kenya? Since these banks derail from the procedures of customary faith on the recompense of interest on the sum loaned out, the capital edifice in shariah complaint banks is an incident that justifies continuity and ascertains the foundations embraced by these banks to obtain funds. One of the goals of the administration is maximizing the banks value, capital structure may affect this value, a suitable and fitting structure which capitalizes on this
worth, and henceforward this study will try to discover out the appropriate capital structure utilized in escalation of the revenues of the bank.

1.3 Objective of the study
This study was guided by the following objective:

1.3.1 General Objective of the Study
To analyze capital structure on the financial performance of Islamic banks in Kenya.

1.3.2 Specific Objectives
The specific objectives are:

i. To determine the relationship between the size and financial performance of Islamic banks in Kenya.

ii. To establish the effect of the age of a firm on the financial performance of Kenyan Islamic banks.

iii. To examine the bond between the firm’s asset tangibility and financial performance of the Kenyan Islamic banks.

iv. To identify the relation between the bank growth opportunity and financial performance of the Kenyan Islamic banks.

v. To assess the relationship between financial leverage and financial performance of the Kenyan Islamic banks.

1.4 Research questions
The following are the research questions

i.) What is the relationship between the size and financial performance of Islamic banks in Kenya?
ii.) What is the effect of age of a firm on the financial performance of Kenyan Islamic banks?

iii.) What is the bond between the firm’s asset tangibility and financial performance of the Kenyan Islamic banks?

iv.) What is the relation of the banks growth opportunity and financial performance of the Kenyan Islamic banks?

v.) What is the relationship between financial leverage and financial performance of the Kenyan Islamic banks?

1.5 Significance of the study

There is a substantial work of academic papers and studies on the influence of capital structure on firm’s performance and research remains to integrate the prevailing theories. This work aims at providing pragmatic proof in approving the cogency of the theories to support the organization’s administration in shaping the best capital structure. The researcher anticipates that the discoveries from the Study shall be useful to the following stakeholders:

Management of companies which will benefit and they will make excellent financial judgments based on the understanding of how capital structure influences a firm's financial performance. Secondly, it will create awareness of Islamic bank’s financial locus and contrast of performance amid Islamic and Conventional banks will be made in order to identify, which one is enhanced financial spot. Thirdly, the government of Kenya as well as the Central Bank of Kenya needs to understand the drivers of performance of the banking sector. Knowledge of such factors that drive performance will inform policy and regulations
that will enhance and safeguard the performance of banks, which are important for stability of the financial markets and the growth of the economy. Fourthly, the banking industry lobby has a keen interest of ensuring that its members are in good financial health to ensure the health of the entire sector. To achieve this, KBA will provide guidelines and rules to be observed by its membership to ensure a sound banking sector. The study may well be of assistance to intellectuals and Einstein who might desire to use its discoveries as a root for further research on capital structure. Last but not least Investors who may need to know the connection between capital structure policy and performance of the IBs for them to elect which company to invest in and as a result shun impetuous venture decisions.

1.6 Scope of Study

This study focused on performance among Islamic banking institutions in Kenya. Throughout the study, capital structure variables were used as the factors to determine the result of performance. Pure Islamic banking institutions were chosen as selected organization for target population since it is quite new in Kenya. This study took 5 years (2011-2015) of performance by looking at its annual financial report that was collected from data stream. It is vital to notice that in this era of study, Republic of Kenya toughened political fretfulness, resulting in indecision within the stock exchange and the general elections held in 2013 were the first under the Constitution of Kenya 2010 and ushered in a major transformative devolved governance system of 47 county governments. Since then, the government has been putting in place various legal, regulatory frameworks and the
relevant supporting institutions aimed at implementing the constitutional provisions for successful implementation of devolution.

1.7 Limitations of the Study
There are a few Islamic banks available in the commercial banks in Kenya that are fully fledged Islamic banks and only a few have a window of Islamic banking. The government can allow more new players to make the market more competitive. Islamic banking is still pretty new in the Kenyan market with just about ten years since commencement. Hence, the results are representative of a banking sector that is still in the growth phase.

The study has vibrant and anticipated limitation within the quantity of knowledge that was used, as a result of the researcher solely used information from record and profit-and-loss statement throughout the period (2011-2015). This project solely centered on the problems rose within the analysis query. This study was built on secondary data collected from Islamic Banks of Kenya. For that reason, the standard of the work rest on strictly upon the exactitude, dependableness and excellence of the secondary information sources. Estimate and comparative measure with regard to the information supply would possibly impact the results. The findings from this study thus aren't generalizable to alternative countries outside Kenya. This is often as a result of alternative countries have discourse and regulative factors that are completely dissimilar from the settings in Kenya and thence explicit studies got to be dole out to ascertain the tie concerning capital structure and financial performance of banks in such realms. The study results are also restricted in illustrating how capital
structure influences performance in alternative sectors in Kenya. This is as results of the other segments are very completely different in however they combine their capital for optimum performance. Because of time constraint this study narrowed right down to five capital structure variables. There are alternative capital structure variables that have an effect on financial performance of listed Islamic banks in Kenya; examples are liquidity and risk that are left out to be examined by other scholars.

1.8 Study Organization

This project is structured as follows: the preceding chapter one provides the analysis background, analysis objectives, analysis queries, worth of the study, scope, and also the limitations encountered within the course of the study. Chapter 2 presents literature review on the capital structure and financial performance of Islamic banks in Kenya, and a conceptual framework. Chapter 3 deals with the methodology utilized within the study; the study findings and also their interpretation are given in chapter four; whereas chapter 5 has conclusions of the study and the policy implications.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction
This section provides theoretical and empirical literature relevant from publications on topics related to the research objectives. Three theories discussed are capital structure irrelevance theory, agency cost theory and trade-off theory. It gives an account of different academic work and evidence from other scholars who have passed out their study in the identical area and the conceptual framework.

2.2 Theoretical Review
So as to attain the intents of the funding of any corporation, the funding process ought to be suited in accordance with the firm goals, which it is over the selection of the ideal mix of financing. A wide range for optimal capital structure can be obtained from academic research but it is not as easy as ABC for any financial manager to find out exact manner which will help in defining most favorable financing mix. Nevertheless in order to understand this more vividly then the study of capital structure theories is essential to know how this merge will have a force on the value of the organization. The main theories discussed in this study are: the Capital Irrelevance Theory, Agency Cost theory, the Tradeoff theory and the Pecking order theory.
2.2.1 Capital Structure Irrelevance Theory

In 1958, Modigliani and Miller proposed Capital Irrelevance Theory and made the foundation to consider regarding capital structure by studying the consequence of wealth structure on company’s value. They recommended that in faultless market, the organization’s worth isn’t moved by its choice of capital structure that is it is not affected by issuing stocks or selling debts.

Huge figures of theoretical and empirical papers were developed after Modigliani and Miller's classical paper (1958). Chosen listed companies were examined by these papers. His work is based under deterring assumptions that the significance of a company is liberated from its financial structure. These suppositions contain the dealings and bankruptcy costs, equivalence of lending and borrowing rates, absence of taxes and in conclusion the freedom of the productive activities of the firm from its financing decisions. Succeeding the classical work, the theoretical and pragmatic capital structure studies have stretched to include supplementary features, such as agency costs, bankruptcy cost, asymmetric information issues and taxes. This assumption points out there is no association between a corporation’s financial structure and its financial performance measures and it contradict the opinion in this study which is the subsistence of an outcome of capital structure on financial performance of a firm. This theory has been reviewed thus on anchor the dependent variable of economic performance. The idea explains that beneath classical stochastic process, and in an economical market, financial performance of the firm is unaffected by however that firm is supported instead, it solely changes the allocation of money flows between debt and
equity, while not ever-changing the entire money flows of the firm (Berk & DeMarzo, 2007).

### 2.2.2 Agency Cost Theory

The first to proposition Agency Cost Theory were Jensen and Mackling (1976). This theory assume that there are dual sorts of conflict of interest; one the conflict concerning the owners and managers and two between the bondholders and shareholders. As for the first conflicts, it crops up owing to the rationale that administrators make resolutions in their own self-centeredness which aren’t similar with the intend of making best use of shareholders wealth. While the conflict between the bondholders and shareholders, takes place as a result of having different approach for expected return and risk. Bond owners have concern in existing profit for its assurances their proceeds while shareholders are prepared to surrender their current returns so as to get long-standing increase in capital. This crafts an agency problem. This theory obtains its foundation on the diverse outline of capital structures that exist in a corporation, as well as the various financial performance measures. It illustrates that with different pick of capital structure then a dissimilar effect on financial performance is expected. This theory has been revised thus on anchor the freelance variables of financial leverage and asset tangibility. This theory apply angst on managers conflict of interest to hunt equity even once profitable growth prospects don't occur, so such income are often used for gratuities instead of for enhancing firm worth. Managers wish free money to speculate in unbeneﬁcial projects that spawn money so salaries or a perquisite is also increased instead of service debt (Calabrese, 2011). This theory but offers resolution by closing that growing leverage would enact financial discipline on administration in such
surroundings. The palpability of assets is additionally thought of as a capital structure determinant in line with the agency theory. Rajan and Zingales (2001) argued that such assets, by acting as collateral for debt, cut back the chance of agency costs related to debt incurred by the soul, and consequently result in a rise in leverage.

2.2.3 Trade-Off Theory

Trade-Off theory of Myers (1977) stipulates that, after bearing in mind the nature and prerequisite of a business, a firm duty is to outline an objective for its debt-equity ratio and then put its sweat in achieving that target. The theory advocates for debt financing since it presents more gain to a business than to equity financing. As for debt financing one acquires tax protection on interest rewarded on debt while for equity financing, profits is indicted with tax. The significance of this theory to this study is that we expect to have a bond concerning financial performance and capital structure. This concept has been appraised thus on anchor the independent variable of Firm’s size. The trade-off theory put forward that managers merely like debt (Myers, 2001). They proportion the costs and edges of liability to succeed in an optimum leverage level; the disbursal on the dues is tax deductible, thus dipping the real worth of using debt comparative to equity (Myers, 2001). Secondly, it implies that giant companies have additional debt in their capital structure and therefore the size of the firm affects the quantity of leverage that the firm would possibly value more highly to select in its capital structure. The implicit anticipation is that enormous corporations ought to have higher debt ratios and little firms ought to take lower debt levels (Gracia & Mira, 2008)
2.2.4 Pecking order theory

The pecking-order theory argues that, attributable to info spatiality, companies’ value more highly to use their maintained earnings initial to finance their investments (Myers and Majluf, 1984). Once internal funding doesn't satisfy, firms issue debt first and equity last. It advocates that companies have a specific fondness order for capital accustomed funding their businesses (Myers and Majluf, 1984). According to Graham and Harvey (2001) most managers ensure that debts are issued once their internal funds are shy to fund their activities. Generally a firm’s inability to get funds using debt affects their choices to issue ordinary shares (Graham and Harvey, 2001). There’s weak support for either the trade-off or the knowledge asymmetry-based pecking-order theory of capital structure, (Graham and Harvey, 2001).

It is therefore as to anchor the independent variables of growth opportunities and firm’s age Pecking order theory, differing to the agency cost theory, displays the constructive relation amongst the growth opportunities and debt level of enterprises. Typically often supported the reasoning that a far better growth probability implies a far better claim for funds, and, on the whole, a bigger dependence on external funding through the favored supply of debt...
While the firm’s age By virtue of the theory in the first steps of their life cycle (Commencement and growth) the firms use debt strategy because of lack of accumulated profit for investment, but they use the debt strategy less in maturity step because of profit increase and when they entered into the decline step again they use the strategy more because of the accumulated profit decrease, (Myers, 2001)
2.3 Empirical Review

The association amongst the capital structure and worth of the corporations is a substance of nice dispute. On the hypothetical level, the argument is there concerning on whether or not the magnitude relation of debt treatment is germane or ill-chosen to individual firm’s worth. On pragmatic level, for standard banks the correlation regarding capital structure and financial performance is closely checked out (Berger and di Patti, 2002; Eriotis et al., 2002; Hutchison and Cox, 2006). Yet still there's a paucity of studies for IBs in Kenya.

2.3.1 Determinants of Capital Structure

Decisions are always of great importance at any particular place and environment. It doesn’t matter whether it is in a household or a business surrounding or regarding an individual in general. Planning is vital so as to have a diplomatic and silky future, as for the firms an unplanned capital structure forbids a proficient utilize of funds for the business. The minute it comes to what kind of capital structure a company ought to have, a clear conscious is needed because of how decisive and imperative it is to the success and solvency of the firm. The firms’ most favorable capital structure will lessen the organization's general cost of capital. Conversely, till to date there are wiles about whether an finest capital structure truly exists. What is the best mix of the funds to be used and how much is the affect to its valuation (Beasley & Brigham, 2000, Ross et al., 2002).

There are countless studies that examine the factors affecting the capital structure just to mention are few like Bevan and Danbolt (2000), Myers (1984), Hall et al., (2004), Antonion et al., (2002), Booth et al., (2001), Buferna et al., (2005), Huang and Song (2002),
Caesar and Holmes (2003), and Chen (2004). As per to the above mentioned studies, the major contributing factor of the capital structure are: growth opportunities, size of the company, long-term debt, profitability, short-term debt and tangibility. Results have been generated by both empirical and theoretical capital structure studies so as to enlighten on the factors affecting the capital structure and some extensive classes of capital structure determinants have surfaced. As for this study will take the following as the variables;

2.3.1.1 Size of the firm

The size of the firm shakes its financial performance in many ways. Huge corporations will use economies of scale and scope and therefore being a lot of competent compared to little corporations. Additionally, tiny corporations could have less power than massive firms; thus they will realize it troublesome to become giant, resulting in inferior financial performance, (Majumdar, 2014).

Size has vital statistical control on financial performance of corporations. This is often reinforced by Tarawneh (2006) establish that the banks with high deposits, total capital, total assets, or credits doesn’t forever suggests that has fatty gain performance. The operational efficiency and asset management, addition to the size of the bank, fully swayed the financial performance of these banks. Within the light-weight of his experimental study he finished that the operational efficiency and asset management, to boot to the bank size, powerfully and fully predisposed financial performance of the banks.
Kuo (2000) studied fifteen domestic public and private banks, and twenty one native outlets of overseas banks in Taiwan from 1989 to 1994. He established important variations in their capital structure proposing that banks embrace totally dissimilar claims of financial leverage. Kuo inveterate direct relationship amongst size of the bank and financial leverage, whereas fixed assets to deposit ratio and variance coefficient of working proceeds are adversely related. A different study by Çağlayan and Şak (2010) who studied the causes of capital structure of banks in Turkey over the age 1992-2007 establishes size and market to book value have constructive effect; whereas tangibility and profitableness have undesirable influences on the book leverage all told times.

Siam et al. (2005) surveyed determining factor of twelve Jordanian banks' from 1992 to 2001 and they resolved bank size, retained earnings, liquidity ratio and long & short term debts to be factors of leverage. They conjointly found a constructive liaison between bank's leverage to its age as well as the total assets and alternatively learned an adverse affiliation amid the bank's leverage to liquidity ratio. Al-Qudah (2014) reported a constructive and vital eventuality on total liabilities to equity ratio, book leverage and market leverage and showed that size includes an encouraging inconsequential influence on deposit leverage and non-deposit leverage in his study of factors capital structure of banks. He conjointly exhibited that market to book ratio includes a recommendatory and vibrant effect on utterly unalike leverage measures he employed in his study except non-deposit leverage.

Baral (2004), in his study determinant of capital structure of financial establishments in Kingdom of Nepal security market in 2003; delivered proof that bank size has a vital effect
on financial leverage; growth rate having an affirmative relationship with leverage ratio and resolute that financial institutes care less of their debt provision capability but do care on the growth of their companies. (Basnet, 2015) wanted to find out whether contributing factor like size, assets corporeality, profitability, collateral, inflation, GDP growth and business risk dividends influence the capital structure of Nepalese developed banks. He resolved that capital structure theories are complementary for the Nepalese business banks and determinants have an effect on the market leverage of the banks.

According to the study by Pratomo and Ismail (2007) there is a pessimistic outcome between the size of the firm and the banking financial performance. Quantity in aspect of the employees is a core variable. With good appraisal and good pay employees are expected to perform tremendous on the other hand to reduce the risk. This study size is an independent variable, and a measured variable SIZE, is introduced as an alternative for size of the firm.

2.3.1.2 Firm’s Age

Many scholars agree that the age of the firm determines the growth of the firm. According to Abdullah, Ismail, Uli & Che Rose (2010), firms that are old in the line of business perform better than the firms which are fresh. This is because as times goes by, the hazard rate descends with time and firm survival in the setting increases with the firm existence in the setting (Person, 2004). Shumway (2001), reports that economically the foremost substantive degree of firm’s age is that the range of years since register. That event may be a shaping moment in an exceedingly company’s life. Not amazingly, listing affects tenure and capital
structure, multiplies growth opportunities, will increase media exposure, and demands totally different company governance structures (Loderer & Waelchli, 2010). Most studies that consider firm age, together with Shumway (2001), Pástor and Veronesi (2003), Fama and French (2004), and Chun et al. (2008), measure age within the same method.

The rapport amid profitability and firm age is argumentative; some testified the optimistic and vital relationship among age and profitableness (Halil & Hassan, 2012; Papadogonas, 2007; Akinyomi & Olagunju, 2012). Others have according undesirable relationship (Majumdar, 1997; Dogan, 2013 and Coad, Segarra & Teruel, 2007). This varied response has created the controversy indecisive.

Loderer and Waelchli (2010) scrutinized the link between firm’s age and performance employing a knowledge set comprising of 10,930 registered USA corporations from 1978 to 2004. Their experiential outcomes indicated that as corporations become big, their ROA, Tobin’s Q, and profit margins ratios deteriorate. Dissimilar to that, Coad et al. (2013) established that older corporations fancy higher yield and profits as observed in between firm age and performance in Spanish producing corporations in 1998 to 2006. Ghafoorifard et al. (2014) their proof disagreeing analyzed the link between age, size of the firm and financial performance in ninety six listed organizations registered on Tehran secutity market from 2008 to 2011 and acknowledged a constructive bond between a firm’s age and its Tobin’s Q ratio. A positive relationship between firm age and profitableness was conjointly documented by Kipesha (2013) for microfinance establishments in Tanzania and by Osunsan et al. (2015) for SMEs in Uganda.
Gurbuz et al. (2010) on a taster of 164 firm-years for real sector companies from 2005 to 2008 couldn’t validate an affiliation between firm age and ROA. Additionally germane is that the study by Basti et al. (2011) casing the age 2003 to 2006 employing a hundred sixty registered firms in Turkey. Outcomes from the model exhibited a constructive connection concerning profitability and age. Contrariwise, Dogan (2013) established a deleterious relation between firm age and ROA running a multiple correlation on data from two hundred listed firms amongst the years 2008-2011.

Sorensen & Stuart, (2000), maintained that organization inaction operational in recent companies be apt to create them strict and inept to understand changes within the surroundings. Fresher companies, end up procuring a pie in spite of handicaps like brand names, lack of capital and company name with older companies (Kakani, Saha & Reddy, 2001). Older companies are well-versed, fancy superior performance and aren’t vulnerable to the liabilities of age. Additionally enjoy status properties, which license them to net a better brim on sales. Since the age of a firm have a strength on the firm’s performance, so the introduction of a dominant variable, AGE during this study

2.3.1.3 Asset Tangibility

It is presumed, from the speculative purpose of view, that tangible assets are often used as indemnity. Thus greater tangibility takes down the peril of a debtor and will increase the worth of the assets within the case of insolvency. As Both, Demirguc-Kunt & Maksimovic (2001) realized, the additional tangible the firm’s assets, the bigger its capability to issue
secured debt and therefore the less evidence apparent regarding future profits. Therefore a constructive relation between tangible and leverage is foreseen. Among the chief aspects of a firm’s performance, asset tangibility is considered as the core. In most of the literature an affirmative relationship between financial performance and asset tangibility is supported. Akintoye (2008) put forward that a firm which depends on intangible assets will obligate larger outlays of financial distress than the firm which retains large investments in tangible assets.

Empirical studies on investment in fixed assets have demonstrated mixed result based on various sectors. The study by Okwo et al. (2012) assessed the influence of a company’s venture in fixed assets on its operational margin of profit. The study relies on a mockup of four firms within the Nigerian distillery sector over an eleven year amount from 1999 to 2009. The findings of the study was that although the connection between the amount of venture in fixed assets and its impact on the operational profit was positive, the result wasn't statistically vibrant. Therefore, the result didn't recommend any robust positive impact of speculation in fixed assets on the operational profit of distillery corporations in Nigeria. On the opposite hand, the study by Olatunji et al. (2014) scrutinized the impact of venture in fixed assets on profitableness of chosen Nigerian banks. Information were gotten from twelve-monthly reports and books of 13 selected Nigerian business Banks for the amount from 2000-2012. The connection among the dependent variable (Net profit) and independent variables indicated that there was a big relationship between them.
Almazari (2011) using simple regression in the financial performance of seven Jordanian banks from 2005 to 2009 projected the stimulus of variable drawn by; the asset management, bank size and operational potency on financial performance. He testified that higher shareholders’ equity, assets, credits, and total deposits don't necessarily mean that the banks will have higher profitability performance. A connection amongst financial performance and operational potency, asset utilization and asset size exists and was established with multivariate breakdown that financial performance is prominently prejudiced by the mentioned determinants. Akhtar, et al., (2016) in examining the effect of capital structure on banking sector of Pakistan thro profitability, liquidity, tangibility, rate of interest and growth rate using 5 banks yearly information amid 2005 and 2015. The results show that there are affirmative vital affiliations between the financial performance and capital structure. In this study asset tangibility is an independent variable, and a measured variable TAN, is introduced as an alternative for asset tangibility of the firm.

2.3.1.4 Growth Opportunities

In unity both Zeitun and Tian (2007) believes that organizations which have established themselves are able to spawn yield from ventures. An unconventional methodology to profit and growth link, the ‘passive learning model’ of Jovanovic (1982) forecasts that the yearly firm’s growth speed hinges on the precision that managers are competent to prophesy the costs of product. Profits of a firm rest on its effectiveness level. If companies ascertain that they're economical, they nurture and continue. Or else if companies that acquire systematically adverse data they refuse and finally vacate the market (Bhattacharjee, 2005). Consequently, over time larger companies become more proficient and there's less area for
more progress in these companies in terms of viability and development, resulting in a unsystematic method for growth, particularly among loftier companies (Kiani et al., 2012).

Liu and Hsu (2006) notice a major constructive result on the expansion of the companies protective cover (2004) displays that growth and profit have an inclination to performance along for British corporations. Hobarth (2006) outlined that to have high profit corporation then economical capital management, fewer liabilities, and high preserved earnings are among elements a good business is to have. Bottazi et al. (2008) moreover they explore an Italian manufacturing corporations, and note that the profit ratio and firm sales growth is optimistic though scarcely vital. Coad (2007) discerns that operational income joins a concrete and vital result on the growth of firms. Guariglia (2009) statuses that the investments that are financed soundly they project higher yields while those invested poorly generated lower level of return proportions. Niskanen and Niskanen (2007) with the proviso firms with ten workers, a positive impact will be obtainable of upsurge in profit on firm growth. In contrast to, Coad (2010) states an undesirable accord betwixt growth and profit. Markman and Gartner (2002), Sexton, et al. (2000) on the same confirmed an abrogating relationship. Moreover, Bottazi et al. (2008) assert there’s not a stimulating connection between the two (i.e….growth and profit).

As seen on top of each hypothetical and experimental literature tries to seek out solutions to those queries: will growth bring profitability? Or as a result of companies are money-making and plow their profits, they’re capable to progress? Hence introducing a managed variable, GROW, an alternate for growth opportunities in this study.
2.3.1.5 Financial leverage

Leverage is used in capital structure to amplify the risk. Capital structure and leverage are narrowly relating concepts. In choice making process for capital structure, leverage is easily gauged and appraised. Leverage permits bigger possible proceeds to the capitalist than ought to have been attainable, if the investment becomes trifling the probable loss is bigger and the credit capital sum and all accumulated interest on the credit still have to be compelled to be recompensed (Andy et. al., 2002). Correspondingly, Pandey (2010) avow that the financial leverage utilized by an organization is meant to net a lot of yield on the fixed charge funds than their expenses. The additional or shortage can surge or diminution the harvest on the proprietors’ equity. It is levered on top of or beneath the total assets rate of return. Thus, financial leverage is taken into account as a two-edged blade as a result of it offers the capacities of skyrocketing the proprietors’ earnings further as making the perils of loss to them.

Ebaid (2009) researched the capital structure on the performance of companies in Egypt. He used Multivariate analysis technique and established that leverage partakes no bearing on a firm’s performance. Maroko (2014) using Multivariate analysis technique surveyed on capital structure on financial performance of companies registered in capital of Kenya Securities Exchange. The study employed secondary information obtained from monetary reports that were elect using stratified sampling technique. Khan (2012); and Saaedi and Mahmoodi (2011) used multi-dimensional data procedures to research on organization’s capital structure and its performance. Khan (2012) applies a least sq. regression on thirty six industrial corporations in Islamic Republic of Pakistan. Outcomes designate a gloomy
conjunction however not statistical imperative between financial leverage and firm performance. Abdul (2012) conducted an identical study in Pakistan. The study completes that financial leverage includes a vital adverse pertinence with firm and financial leverage firm performance was undesirable however not stats vital. Scilicet, Javed and Akhtar (2012) obtained a constructive tie mid financial leverage, growth, financial performance and size of the businesses. It centered on the city stock market in Pakistan and the outcomes are in line with the agency theory. This study insulated the other funding choices and centered solely on financial leverage. In this study I introduce a managed variable, FIN associate alternate for financial leverage during this study.

2.3.2 Determinants of Financial Performance

Conferring to Al-Tamimi (2010) and Aburime (2005), the bank performances can be impinged on by various elements and these aspects can be categorized into micro and macro factors. These variables verify the productivity. The Inner factors are all factors which define a specific bank character that affects the banks performance either positively or negatively. European financial organization (2010) report has categorized them in to 3 major classes that are ancient, economic and market based mostly measures. the normal measures are almost like those utilized by alternative companies that embody return on Assets (ROA), return of Equity (ROE); this is often the foremost famed measure of financial performance. Performance refers to the flexibility of the banks to breed sustainable profit (Wild, Shaw & Chiappetta, 2009).The in-house influences are inside the range of the bank so as to maneuver them and that they vary within each bank. These factors include things like
management quality, interest rate policy, labor productivity, risk level, capital size, technology, composition and size of credit portfolio, condition of information, size of deposit liabilities, bank size, ownership and the like. The bank’s management uses CAMEL framework to estimate financial strength and performance. CAMEL means Capital Adequacy, Asset Quality, Management Efficiency, Earnings Ability and Liquidity.

The main measure of financial performance is through ratio analysis which has been identified as convenient and efficient method of assessment since it combines information from financial statements and comes up with numbers that are more easily interpreted financial meaning, (Burckhardt, 2013). As for this study ROA and ROE was used as dependent variables.

2.3.2.1 Return on Assets (ROA)

According to Khrawish (2011), ROA is a key quotient in determining the productivity of a bank and it is calculated by dividing Income to its total asset. It shows the capability of the executive of the bank to produce proceeds by using company resources accessible. Videlicet, it displays by what means resourcefully the assets of the bank are used to create the revenue and how the management of the bank is skillful in engendering net income on or after all the capitals of the organization. Wen (2010) states that the developed the ROA the better for the bank and it shows that the bank proficiently uses its resources

Saeed, Gull, and Rasheed (2013) in their paper confirmed an affirmative liaison concerning elements of capital structure and financial performance of Pakistani banking business. The study extended sensible work on determinants of capital organization of banks in Islamic
Republic of Pakistan over the epoch of 5 years (2007-2011) by creating use of information of banks registered on the city securities market (KSE). Multivariate analysis representations of all banks operative in Pakistan were utilized in the study over the age of 2007-2011. Financial Performance was quantified using earnings per share, return on equity and return on assets whereas the independent variables were total debt to capital ratio, short term debt to capital ratio and long run debt to capital ratio.

Another analysis by Gleason et al.(2000) on the relation mid capital structure, culture and performance from fourteen European retailers, exhibited existence of a gloomy alliance betwixt the capital structures of those traders and their ROA, sales growth and pre-tax income. Additionally capital structure speckled by the artistic taxonomy of outlets, but the performance of those traders was in no means passionate about social inspiration overall. Per Amidu, (2007), exhausting ROE & ROA for Republic of Ghana’s firms, he deducted that growing corporations have a prospect of breeding extra yields for the possessors.

According to the research worker information with the exception of (Wang, 2002) who addresses the liquidity management, no studies address this relationship. He investigates Taiwan and Japan companies on the cash flow and its interconnection with performance and spots that the cash conversion cycle (CCC) features a damaging rapport with the financial performance measured by ROA or ROE and this tie is subtle to trade dynamics. Moreover, he catches that forceful capitalization enriches in operation performance.
2.3.2.2 Return on Equity (ROE)

To check on how much profit a company took home weighed against to the full sum of stockholder equity capitalized or established on the book of account is what ROE ratio stands for. ROE in simply words is what the investors anticipate for their venture. A business with a high ROE is competent of spawning cash within. Thus, the superior the ROE the enhanced the bank is in tenures of profit breeding. It is additional clarified by Khrawish (2011) that ROE is the proportion of Net Income after taxes shared by Total Equity Capital. ROE is reflection in what way proficiently the administration of the bank is using savers’ funds hence it can be construed that the healthier the ROE the further effectual the management is in using the bondholders capital. Di Patti and Berger (2002) used a replacement way to assess the results of capital structure on banks’ performance. They used an equation exemplary that explains for reverse causality from performance to capital. Profit was used to measure the firm performance and an agency cost was a controlled measure for capital structure, different bank features, market aspects and directive were conjointly enclosed within the tests. the information of 7,320 U.S.A. banks from 1990-1995 was used, and also the results showed that a diminution in owners’ equity toward chattels ratio by 1% at the model mean entails a lift in ROE of concerning half dozen percent. Their discoveries are dependable with the agency theory and also the outcomes are vital. The study created by Arbiya and safari (2009) acknowledged comparable results, scrutinizing one hundred Iranian publically registered corporations on their performance over the era 2001 to 2007. Short term and total debts were completely associated with profit, however an undesirable relationship between long-term debts and ROE was acquired.
2.4 Summary of Literature Review and Research Gaps

From the above it’s flawless that there have been few research studies or none at all in Kenya apropos the outcome of capital structure on the financial performance of the Kenyan Islamic Banks. This study is meant to fill the gap or add more literature on the subject.

Table 2.1 Tabular Summary of literature review

<table>
<thead>
<tr>
<th>Author(s)</th>
<th>Title of the study</th>
<th>Methodology</th>
<th>Study Population</th>
<th>Time Frame</th>
<th>Study Findings</th>
<th>Identified Gaps</th>
</tr>
</thead>
<tbody>
<tr>
<td>Thomas Gitari Njega</td>
<td>The relationship between capital structure and financial performance of the manufacturing companies listed on the Nairobi stock exchange</td>
<td>descriptive research design</td>
<td>industrialized firms quoted on the Nairobi Securities Exchange Market</td>
<td>2006 to 2012</td>
<td>Major parts of capital structure are debt and equity No important statistical bond amongst capital structure and assets of the manufactured companies and financial gain of the producing corporations quoted on the Nairobi Securities Exchange</td>
<td>A study on establishing the optimal range for capital structure should be undertaken so as to form a good basis for forming decisions relating to the capital structure of businesses.</td>
</tr>
<tr>
<td>Author(s)</td>
<td>Title of the study</td>
<td>Methodology</td>
<td>Study Population</td>
<td>Time Frame</td>
<td>Study Findings</td>
<td>Identified Gaps</td>
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</tr>
<tr>
<td>Doris Kanini</td>
<td>Effects of capital structure on financial performance of commercial banks in Kenya</td>
<td>Empirical research method</td>
<td>33 licensed Commercial banks in Kenya</td>
<td>2005 to 2014</td>
<td>retained earnings, debt and preference shares affects the commercial bank’s financial performance positively while ordinary shares affects the commercial bank’s financial performance negatively</td>
<td>further studies during this space incorporating different financial performance measures like return on equity and incorporating totally different variables from those that are used in this study like impact on level of advertising and promotion, marketing strategies adopted, insurance products innovations, management actions and new product development</td>
</tr>
<tr>
<td>Serap çoban</td>
<td>The interaction between firm growth and profitability: evidence from Turkish (listed) manufacturing firms</td>
<td>Dynamic panel data estimation methods</td>
<td>137 Turkish listed manufacturing firms</td>
<td>1997-2012</td>
<td>A statistically significant positive affinity in profits and growth and no statistically significant association among prior year’s profits and current growth.</td>
<td>The dataset utilized isn’t adequate to simplify the results done in all Turkish manufacturing divisions. altered profit ratios and growth variables is also used to ensure these outcomes</td>
</tr>
<tr>
<td>Author(s)</td>
<td>Title of the study</td>
<td>Methodology</td>
<td>Study Population</td>
<td>Time Frame</td>
<td>Study Findings</td>
<td>Identified Gaps</td>
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<tr>
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</tr>
<tr>
<td>Mwangi, Makau and Kosimbei</td>
<td>Relationship between Capital Structure and Performance of Non-Financial Companies Listed In the Nairobi Securities Exchange, Kenya</td>
<td>Explanatory non-experimental research design</td>
<td>42 non-financial corporations registered in the NSE</td>
<td>2006-2012</td>
<td>financial leverage had a statistically vital deleterious link with performance as measured (ROA) and (ROE</td>
<td>A study ought to be carried out to check the financings adoptions of non-monetary firms registered on the NSE and those ex-directory and therefore the effects of those choices on performance. Additionally, forthcoming studies may well be stretched to research fiscal resolutions and their bearing on performance across the countries particularly those within the East African Community.</td>
</tr>
<tr>
<td>Mohammed Getahun</td>
<td>Determinants of capital structure and its Impact on the performance of Ethiopian Insurance industry</td>
<td>descriptive statistics</td>
<td>All insurance corporations were enclosed within the model setting if they had 10 years yearly report</td>
<td>2004-2013</td>
<td>A significant adverse link is recognized concerning leverage and performance</td>
<td>use other indicators for determinants, new hypotheses and new variables to reinvestigates their relationships and to reflect the effect on firm performance interrelated with concept of capital structure</td>
</tr>
<tr>
<td>Author(s)</td>
<td>Title of the study</td>
<td>Methodology</td>
<td>Study Population</td>
<td>Time Frame</td>
<td>Study Findings</td>
<td>Identified Gaps</td>
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<tr>
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</tr>
<tr>
<td>Fredrick Boro Kuria</td>
<td>The effect of capital structure on the financial performance of commercial banks in Kenya</td>
<td>A descriptive study design</td>
<td>35 viable banks in Kenya</td>
<td>2008 to 2012</td>
<td>there is no substantial rapport amid the capital structure and the financial performance of commercial banks in Kenya</td>
<td>Identifying other causes which upset the performance of commercial banks. Use other methods of financial performance such as return on assets instead of return on equity. Use different variables from those which have been used in this study.</td>
</tr>
<tr>
<td>Ayanda, Christopher, Adedoyin and Mustapha</td>
<td>Determinants of Capital Structure in Nigerian Banking Sector</td>
<td>Pooled ordinary Least Square (Pooled OLS) technique</td>
<td>5 biggest banks</td>
<td>2006 to 2010</td>
<td>The main determinant are mainly bank size, dividend payout, profitability, tangible assets, growth, business risk and tax charge factors</td>
<td>Future studies should increase the length of the research period of the study to ensure that there is no biasness in drawing up samples for conclusions.</td>
</tr>
</tbody>
</table>


<table>
<thead>
<tr>
<th>Author(s)</th>
<th>Title of the study</th>
<th>Methodology</th>
<th>Study Population</th>
<th>Time Frame</th>
<th>Study Findings</th>
<th>Identified Gaps</th>
</tr>
</thead>
<tbody>
<tr>
<td>Elif Akben-Selcuk</td>
<td>Does firm age affect profitability? Evidence from Turkey</td>
<td>A fixed effects model</td>
<td>302 non-financial firms</td>
<td>2005 to 2014</td>
<td>An adverse and protuberant liaison amongst firm age and Profitability measured by return on assets, return on equity or gross profit margin</td>
<td>The descriptive power of the regression models wasn’t very high because Data restraints required the author to ponder a limited number of explanatory variables</td>
</tr>
<tr>
<td>Mathewos Woldemariam Birru</td>
<td>The Impact of Capital Structure on Financial Performance of Commercial Banks in Ethiopia</td>
<td>Quantitative research approach</td>
<td>8 banks</td>
<td>2011 to 2015</td>
<td>DR, DER, SIZE and TANG have statistically substantial elements upsetting financial performance measured by return on assets and return on equity and LD is statically inconsequent ial with its particular nature of impact</td>
<td>exploration in the connection flanked by capital structure and financial performance are indecisive and necessitates additional Experimental works.</td>
</tr>
<tr>
<td>Author(s)</td>
<td>Title of the study</td>
<td>Methodology</td>
<td>Study Population</td>
<td>Time Frame</td>
<td>Study Findings</td>
<td>Identified Gaps</td>
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<tr>
<td>Abdelrhaman Ahmad Meero</td>
<td>The Relationship between Capital Structure and Performance in Gulf Countries Banks: A Comparative Study between Islamic Banks and Conventional Banks</td>
<td>Descriptive and T test analysis</td>
<td>16 GC Banks (8 Islamic Banks and 8 Conventional Banks) for the period</td>
<td>2005-2014.</td>
<td>ROA as performance measurement moreover has a constructive liaison with equity to assets ratio. These findings Result analysis validates a positive relationship between ROA as performance measurement is undesirably linked to the financial leverage</td>
<td>The research study ought be done in other emergent countries to confer with the discoveries</td>
</tr>
<tr>
<td>Robert Oginda Siro</td>
<td>Effect of capital structure on financial performance of firms Listed at the Nairobi securities exchange</td>
<td>Longitudinal research design,</td>
<td>61 listed firms</td>
<td>2012</td>
<td>an antithetical rapport concerning capital structure and financial performance of registered firms in securities exchange in Kenya</td>
<td>constricted based study casing a precise segment or company be done to discover out the Bearing of Capital Structure on Performance</td>
</tr>
<tr>
<td>Author(s)</td>
<td>Title of the study</td>
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<tr>
<td>Mwaniki and Omagwa</td>
<td>Asset Structure and Financial Performance: A Case of Firms Quoted Under Commercial and Services Sector at the Nairobi Securities Exchange, Kenya</td>
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<tr>
<td></td>
<td>Methodology: descriptive research design</td>
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<tr>
<td></td>
<td>Study Population: seven firms</td>
<td></td>
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<tr>
<td></td>
<td>Time Frame: 2010 to 2014</td>
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<td></td>
<td>Study Findings: Asset structure had a significant statistical consequence on the financial performance. Current assets and intangible assets don’t have statistical implication on financial performance.</td>
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<td></td>
<td>Identified Gaps: Create models that can explain their relationship and determine their effect on the financial performance. The study was conducted on one sector of the firms listed at the NSE, and therefore the results can’t be comprehensive to others firms in the other sectors of the economy due to contextual differences.</td>
<td></td>
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<tr>
<td>Maysa’a Munir Milhem</td>
<td>Banks Performance and Capital Structure: Comparative Study between Islamic Banks and Conventional Banks</td>
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<tr>
<td></td>
<td>Methodology: descriptive research design</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Study Population: 16 banks, 3 Islamic banks and 13 conventional banks</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Time Frame: 2010-2015</td>
<td></td>
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<td></td>
<td>Study Findings: Capital structure shakes financial performance of the Jordanian Islamic banks meaningfully, while there isn’t statistically noteworthy outcome of capital structure on Jordanian conventional banks performance.</td>
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<td></td>
<td>Identified Gaps: The study scans the bearing of capital structure on performance of Islamic Jordanian banks devoid of equating this effect with conventional banks in Jordan</td>
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</tbody>
</table>
2.5 Conceptual Framework

To provide the bond connecting the firm financial performance and capital structure, a conceptual framework is developed to assist in analyzing data. The conceptual framework below represents the connection amid capital structure and financial performance of Islamic banks in Kenya.

**Independent variable**

- Size of the firm
  - Sales turnover
- Age of the firm
  - the number of years since establishment
- Asset Tangibility
  - Net fixed Assets / Total Assets
- Growth Opportunities
  - Company’s revenue over the same period/ total revenue in an industry over the same period
- Financial leverage
  - Total Debt / Total Equity

**Dependent variable**

- Financial performance
  - Return on Assets (ROA)
  - Return on Equity (ROE)

**Figure 2.1 Conceptual Framework**

Source: Author, 2018
CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This section presents the method employed in the study. It identifies, define and provide justification for the research strategy practiced in the study. It as well discusses the data compilation instrument and population that were identified along with sampling frames, techniques and the size for the study and lastly the data analysis methods that were employed.

3.2 Research Design

This study espoused an explanatory non-experimental research design to analyze the consequences of funding choices on performance of Islamic banks, Kenya. Explanatory research tries to find to ascertain fundamental relationship among variables, Non experimental research comprises variables that aren’t influenced by the scientist and instead are studied as they exist. (Saunders et al., 2009 & Robson 2002) Kerlinger and Lee (2000) stated that an explanatory non-experimental research design is suitable where the canvasser is cracking to elucidate how the occurrence functions by ascertaining the basic aspects that yield change in it in and on the other hand no interference of the self-regulating variable. This study employs quantitative methods of performing research, which have been adept, as endorsed by management studies in the developing countries. Cooper and Schindler (2009) went ahead and argued that Descriptive studies are also steered to validate links or relationships between things in the world around us. These are the aims of this study.
Consequently this study is explanatory non-experimental looking for to institute the association amid funding resolutions as well as performance.

3.3 Target Population

This study’s population comprised of 2 completely developed Islamic banks in Kenya. That is Gulf African Bank of Kenya and First Community Bank As at December 2015. The study utilized yearly statistics from the Central Bank and banking association and the yearly reports for shariah complaint banks for the epoch from 2011-2015. This passé is well thought out adequate enough given time restraint over which the study was steered. Abor (2005) analysis of effect of capital structure on profitability of registered corporations in Ghana used a 5 year capaciousness exhausting data from Ghana Stock Exchange amid 1998 and 2002.

3.4 Sampling Technique

According to Collins and Hussey (2006) sampling technique is a method used in selecting elements from the population that will represent the population. Whether a particular technique is of simple random type or different type, it depends on a variety of factors such as object, scope and nature of the study (Hyers, 2006). For this study, non-probability sampling technique was used, that is, purposive sampling. In this study, a selective sample of two fully fledged banks was taken from the population. The selected sampling method ensured precise information that respond to the specific research objectives thereby enhancing the credibility and reliability of the findings of this study (Cooper and Schindler, 2003).
3.5 Data Collection Instrument and Procedure

Cooper and Schindler (2014) state that gathering of information could vary from an easy observation at a location to a grand survey of international firms at sites in numerous components of the globe. The tactic chosen can mostly verify however information is collected. Information is outlined as the facts bestowed to the researcher from the study’s setting. Data reflect their truthfulness by closeness to the phenomena. This study relied on available secondary data sources Saunders et al. (2003) assert that secondary data include both raw and published summaries. The data used was retrieved from the Islamic banks financial reports. The financial declarations which constitute of income statements and statements of financial position of the two full-fledged Islamic banks in Kenya were the focal resources of facts for this study. Therefore this study exclusively used secondary data to address the proposed research objectives. The research tool for data collection was secondary data collection guide – (Appendix 5.)

3.6 Data Analysis and Presentation

According to Cooper and Schindler (2014) the primary step in information preparation is editing. Editing distinguishes booboos and omissions, rectifies them once doable, and indorses that most data quality criteria are earned. Coding encompasses assigning numbers or symbols to responses so answers are often classified into a restricted number of programs. Information entry converts data gathered by secondary or primary strategies to a medium for viewing and manipulation. Descriptive tools are used for cleansing data, discovering issues, and summarizing distributions. A distribution (of data) is associate array of value counts from lowest to highest value of a variable, ensuing from tabulation of incidence.
Descriptive statistical measures were used to depict the middle, spread, and form of distributions and are useful as preliminary tools for data description. Inferential statistics measures were used to check specific objectives. The study adopted the use of statistical Package for Social Sciences (SPSS) that is an {appropriate} software system applied to scrutinize the info through appropriate statistical tools, including descriptive statistics, Kolmogorov-Simonov check and linear regression model.

3.7 Empirical Model and Measurement of Variables

Empirical models are those that are supported entirely on data. These models are not derivative from postulations pertaining to the relationship between variables and they aren’t bottomed on physical doctrines. Regression analysis was conducted out to exam impression of capital structure on financial performance of the Islamic banks. In this study financial performance was the dependent variable and Capital structure was the independent variable. As of these independent and dependent variables, these relations were invented.

\[
ROA_{it} = \alpha + \beta_1 SIZE_{it} + \beta_2 AGE_{it} + \beta_3 TANG_{it} + \beta_4 FIN_{it} + \beta_5 GROW_{it} + \epsilon_{it} \ldots \ldots \quad (1)
\]
\[
ROE_{it} = \alpha + \beta_1 SIZE_{it} + \beta_2 AGE_{it} + \beta_3 TANG_{it} + \beta_4 FIN_{it} + \beta_5 GROW_{it} + \epsilon_{it} \ldots \ldots \quad (2)
\]

Where:
- \(ROA_{it}\) = Return on assets of company \(i\) at time \(t\)
- \(ROE_{it}\) = Return on equity of company \(i\) at time \(t\)
- \(SIZE_{it}\) = size of the company (measured as sales turnover) of company \(i\) at time \(t\).
- \(AGE_{it}\) = firm’s age of a company \(i\) at time \(t\).
- \(TANG_{it}\) = asset tangibility of a company \(i\) at time \(t\).
- \(FIN_{it}\) = Financial leverage of firm \(i\) at time \(t\)
- \(GROW_{it}\) = Growth opportunity of a company \(i\) at time \(t\)
\[ \alpha = \text{Constant term} \]
\[ \beta's = \text{coefficients of the explanatory variables} \]
\[ \epsilon_{it} = \text{composite error term} \]

While the independent variables were measured as follows:

**Table 3.1: Variable Measurement Table**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Measurement</th>
<th>Some reference</th>
<th>Expected sign</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>SIZE OF THE FIRM</strong></td>
<td>Sales Turn over</td>
<td>Molyneux and Gardener (2004), Yudistira (2004),</td>
<td>+</td>
</tr>
<tr>
<td><strong>AGE OF THE FIRM</strong></td>
<td>Number of years since establishment</td>
<td>(Person, 2004). Shumway (2001),</td>
<td>+</td>
</tr>
<tr>
<td><strong>ASSET TANGIBILITY</strong></td>
<td>Net fixed Assets/Total Assets</td>
<td>Gaud <em>et al.</em>, 2005, Fattouh, Scaramozzino, &amp; Harris 2005</td>
<td>+</td>
</tr>
<tr>
<td><strong>GROWTH OPPORTUNITY</strong></td>
<td>Company revenue of the same period / Total revenue of the sector of the same</td>
<td>Zeitun and Tian (2007)</td>
<td>+</td>
</tr>
<tr>
<td></td>
<td>period</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>FINANCIAL LEVERAGE</strong></td>
<td>Total Debt/Total Equity</td>
<td>(Abor, 2005; Ebad, 2009).</td>
<td>+</td>
</tr>
</tbody>
</table>
CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction
This section presents the outcome of the data analysis and the answers from this study in correspondence to the research purposes and in coherence with the literature appraised in part two. The secondary data attained from the financial reports of the banks were analyzed. The bond amid the variables was established by regression analysis. The results were construed as per to the research goals.

**Figure 4.1: Trends of ROA**

Source: Author 2017.

The figure above shows the trends on return on asset (ROA) of the two developed Islamic banks in Kenya i.e. Gulf African Bank (GAB) and First Community Bank (FCB) as from 2011 to 2015. As from 2011 the graph shows an improving trend on GAB’s ROA. It is
evident that the overall trend was consistently upward while ROA of FCB first year it was up then it showed a downward trend throughout the period.

**Figure 4.2: Trends of ROE**

Source: Author 2017

The figure above shows the trends on return on equity (ROE) of the two compassed Islamic banks in Kenya i.e. Gulf African Bank (GAB) and First Community Bank (FCB) as from 2011 to 2015. For the ROE of GAB there was a climb in early years then it dropped then it gradually surged to a high of 0.2 while that of FCB the early years there was a soar to almost 0.25 then plummeted to as low as negative.
4.2 Descriptive Statistics

Table 4.1: Descriptive Statistics

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
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<tr>
<td>AGE OF THE FIRM</td>
<td>10</td>
<td>3</td>
<td>7</td>
<td>5.00</td>
<td>1.491</td>
</tr>
<tr>
<td>SIZE</td>
<td>10</td>
<td>1056571.0</td>
<td>9137690.0</td>
<td>2290189.600</td>
<td>2463663.7117</td>
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<tr>
<td>TANGIBILITY</td>
<td>10</td>
<td>.0153214</td>
<td>.0278020</td>
<td>.020140260</td>
<td>.0042218932</td>
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<td>ROA</td>
<td>10</td>
<td>-.01609</td>
<td>.02957</td>
<td>.0115210</td>
<td>.01351436</td>
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<tr>
<td>ROE</td>
<td>10</td>
<td>-.22571</td>
<td>.22387</td>
<td>.0782810</td>
<td>.12703815</td>
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<tr>
<td>GROWTH</td>
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<td>-.0544975</td>
<td>.0077742</td>
<td>-.002960230</td>
<td>.0182427767</td>
</tr>
<tr>
<td>LEVERAGE</td>
<td>10</td>
<td>5.0000000</td>
<td>13.0000000</td>
<td>7.800000000</td>
<td>2.4404006957</td>
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<tr>
<td>Valid N (listwise)</td>
<td>10</td>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

Source: Authors’ compilation, generated using SPSS 2017

The mean ROA of modeled banks is nearly 1.2%, while of the ROE is sort of 7.8%. The results signify as a rule, for each N100 value of the overall assets of the banks, mere N1.2 was created as yield after tax, while N7.8 was obtained as profit after tax on every N100 equity share given. The return on assets average value for ten observations was 0.115210 with a regular deviation of 0.01351436 and lowest and highest values of -0.01609 and 0.02957 correspondingly. The return on assets was positive showing that the banks were on the average profitable though one amongst the banks was acting at a loss as replicated within the negative minimum monitored value of return on assets. The come back on equity mean value was 0.0782810 with a regular deviation of 0.12703815 and least and ceiling values of -0.0544975 and 0.0077742 severally for ten observations. The demoralized minimum value observation for return on equity implies that one amongst the companies was operational at a failure.
From the outcomes output exhibited in table one, the financial leverage mean value was 7.8. This points out that, on middling, the Islamic banks were extremely geared. the best extent of their sources was supported by long run debt. the standard deviation of 2.4404 points to a minute variation in financial leverage as supported by the very fact that the lowest viewed financial leverage was five whereas the higher limit was thirteen.

The results in table 1 further indicate that, GROW (growth opportunity) had a mean value of -0.00296023 with lowest and utmost values of -.0544975 and 0.0077742 in that order. This scrutiny shows that one the company is not making profit that is why we have a minimum of negative. These results suggest that the rate at which it is growing it’s so small. However the maximum, value of 0.0077742, indicates that there was a company that had a steady growth meaning it was realizing profits from its operations and slowly gaining popularity.

The end result revealed in table 1 designate that the mean value of net fixed assets to total assets ratio (TANGIBILITY) was 0.02014026 with smallest amount and most values of 0.0153214 and 0.0278020 respectively. The mean value indicates that, on common, banks were neither very insistent nor markedly conformist in their investing on assets. Tangible assets have long been used to assess the worth and verify the aggressiveness of any enterprise within the market place. It’s so unimaginable for any enterprise to not have a listing of its tangible assets.

The output exposed in table 1 specifies that the mean value of SIZE is 2290189.6 for both banks which are in the category of small according to Kenya central bank report, 2015. Finally, the mean for the AGE (the number of years since establishment) for the firms under
consideration was 5, literally meaning that the firms are still very young in the industry when comparing with other banks that have been in the field for almost 90 years.

4.3 Regression Analysis

Multivariate regression analysis was used to scrutinize the degree to which explanatory variables captured in the model contribute to the elucidated inconsistency in the dependent variable. The analysis study sought-after to create the influence of capital structure on financial performance of the Islamic banks in Kenya.

Table 4.2: Model 1 Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.991a</td>
<td>.982</td>
<td>.959</td>
<td>.00273893</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH

Source: Authors’ compilation, generated using SPSS 2017

Table 4.3: ANOVA table for model 1

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.002</td>
<td>5</td>
<td>.000</td>
<td>43.023</td>
<td>.001b</td>
</tr>
<tr>
<td>Residual</td>
<td>.000</td>
<td>4</td>
<td>.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>.002</td>
<td>9</td>
<td>.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROA

b. Predictors: (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH

Source: Authors’ compilation, generated using SPSS 2017
In table 2 the results obtained signify that the generally coefficient of determination ($R^2$) displays that the equation has a good fit with 0.982 for ROA meaning that 98.2 percent change in the dependent variable ROA are rooted by the independent variables (FIN, TANG, SIZE, AGE and GROW). The superior the $R^2$, the privileged the goodness of fit and the higher the goodness of fit the higher the reliability of the model. More supportive evidence is obtained in Table 3 where the Sig value helps us to determine if the condition means under study were relatively the same or if they were significantly different from one another the study found out sig value was 0.001. This value was less than 0.05 hence it can be wrapped up that there was statistically significant. Moreover, in Table 4 above the outcomes of multiple regressions exposed that AGE has a negative and weighty consequence on the financial performance by a beta rate of $\beta_1 = -0.009$ (p-value = 0.005 which is not as much of $\alpha = 0.05$). As a result, the researcher discards the null hypothesis and it is acknowledged that for every unit escalation in AGE, there is 0.009 unit decrease in...
financial performance. The consequences demonstrated that the regular measurement beta and p value of SIZE were positive and noteworthy \((\beta = 0.0007, \ p = 0.11 < 0.05)\). As a consequence, the researcher castoffs the null hypothesis and it is recognized that, SIZE has a constructive and momentous effect on performance. Similarly, for every component surge in SIZE, there is 0.0007 unit rise in performance. The results also show that TANG, p-value is significant \((p = 0.019 < 0.05)\), and its beta value was negative \((\beta = -1.872)\). For that reason, the researcher throwaways the null hypothesis and settles that TANG has a negative and substantial influence on the financial performance. Thus, for each entity increase in TANG, there is 1.872 declines in performance. In conclusion, that GROW has a positive and important influence on the financial performance with a beta value of \(\beta_1 = 1.490\) \((p\text{-value} = 0.008\) which is a lesser amount of than \(\alpha = 0.05\)). Thus, the researcher discards the null hypothesis and it is acknowledged that for every one unit growth in GROW; there is 1.490 unit rise in financial performance. The regression model fit is thus:

\[
ROA_t = 0.095 - 0.009 \times AGE_t + 0.0007 \times SIZE_t - 1.872 \times TANG_t + 1.490 \times GROW_t
\]

Table 4.5: Model 2 Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.988(^a)</td>
<td>.975</td>
<td>.945</td>
<td>.02987296</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH

Source: Authors’ compilation, generated using SPSS 2017
Table 4.6: ANOVA Table for Model 2

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.142</td>
<td>5</td>
<td>.028</td>
<td>31.752</td>
<td>.003b</td>
</tr>
<tr>
<td>Residual</td>
<td>.004</td>
<td>4</td>
<td>.001</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>.145</td>
<td>9</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROE
b. Predictors: (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH

Source: Authors’ compilation, generated using SPSS 2017

Table 4.7: Coefficients table for Model 2

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>.828</td>
<td>.232</td>
<td></td>
<td>3.575</td>
</tr>
<tr>
<td>AGE OF THE FIRM</td>
<td>-.080</td>
<td>.017</td>
<td>-.937</td>
<td>-4.790</td>
</tr>
<tr>
<td>SIZE</td>
<td>4.785E-008</td>
<td>.000</td>
<td>.928</td>
<td>2.566</td>
</tr>
<tr>
<td>TANGIBILITY</td>
<td>-18.240</td>
<td>5.398</td>
<td>-.606</td>
<td>-3.379</td>
</tr>
<tr>
<td>GROWTH</td>
<td>12.825</td>
<td>3.322</td>
<td>1.842</td>
<td>3.860</td>
</tr>
<tr>
<td>LEVERAGE</td>
<td>-.007</td>
<td>.010</td>
<td>-.136</td>
<td>-6.79</td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROE

Source: Authors’ compilation, generated using SPSS 2017

In table 5 the results obtained show that the general coefficient of determination (R²) confirmations that the equation has a good fit with 0.975 for ROA meaning that 97.5 percent alteration in the dependent variable ROE are triggered by the self-governing variables (FIN, 60
TANG, SIZE, AGE and GROW). The greater the $R^2$, the upper the goodness of fit and the higher the goodness of fit the higher the reliability of the model. More supportive evidence is obtained in Table 6 where the Sig value helps us to determine if the condition means under study were relatively the same or if they were significantly different from one another. The study found out sig value was 0.003. This value was less than 0.05 hence it can be concluded that there was statistically significant. Furthermore, in Table 7 above the outcomes of multiple regressions exposed that AGE has a negative and weighty result on the financial performance with a beta value of $\beta_1 = -0.080$ (p-value = 0.009 which is not as much of as $\alpha = 0.05$). Thus, the researcher discards the null hypothesis and it is believed that for each component upsurge in AGE, there is 0.080 unit decrease in financial performance. The results also show that TANG, p-value is significant (p=0.028< 0.05), and its beta value was adverse (beta = -18.240). So, the investigator rejects the null hypothesis and determines that TANG has a negative and momentous influence on the financial performance. Accordingly, for every component growth in TANG, there are 18.240 declines in performance. This result indicates that banks invest an excessive amount of fixed assets in an exceedingly manner that doesn't improve their performance, or that they do not use their fixed assets expeditiously, thus it's a negative impact on their financial performance. Finally, that GROW has an affirmative and momentous result on the financial performance with a beta value of $\beta_1 = 12.825$ (p-value = 0.018 which is a reduced amount of than $\alpha = 0.05$). Then, the researcher casts offs the null hypothesis and it is acknowledged that for each one element increase in GROW; there is 12.825 element rise in financial performance. The regression model fit is thus:

$$ROE_{it} = 0.828 - 0.080AGE_{it} - 18.240TANG_{it} + 12.825GROW_{it}$$
4.3.1 Diagnostic Tests

Regression diagnostics are wont to value the model assumptions and investigate whether or not there are observations with an outsized, undue influence on the analysis.

4.3.1.1 Normality Test

Table 4.8: One-Sample Kolmogorov-Smirnov Test

<table>
<thead>
<tr>
<th></th>
<th>AGE OF THE FIRM</th>
<th>SIZE</th>
<th>TANGIBILITY</th>
<th>ROA</th>
<th>ROE</th>
<th>GROWTH</th>
<th>LEVERAGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>N</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Normal Parameters</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Test distribution is Normal.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Calculated from data.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Parameters</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mean</td>
<td>5.00</td>
<td>2290189.600</td>
<td>0.020140260</td>
<td>0.0115210</td>
<td>0.0782810</td>
<td>-0.002960230</td>
<td>7.80</td>
</tr>
<tr>
<td>Std. Deviation</td>
<td>1.491</td>
<td>2463663.711</td>
<td>0.004221893</td>
<td>0.0135143</td>
<td>0.1270381</td>
<td>0.018242776</td>
<td>2.440</td>
</tr>
<tr>
<td>Most Extreme Difference</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Absolute</td>
<td>0.149</td>
<td>0.361</td>
<td>0.213</td>
<td>0.178</td>
<td>0.187</td>
<td>0.462</td>
<td>0.233</td>
</tr>
<tr>
<td>Positive</td>
<td>0.149</td>
<td>0.361</td>
<td>0.213</td>
<td>0.091</td>
<td>0.126</td>
<td>0.278</td>
<td>0.211</td>
</tr>
<tr>
<td>Negative</td>
<td>-0.149</td>
<td>-0.308</td>
<td>-0.127</td>
<td>-0.178</td>
<td>-0.187</td>
<td>-0.462</td>
<td>-0.233</td>
</tr>
<tr>
<td>Kolmogorov-Smirnov Z</td>
<td>0.471</td>
<td>1.140</td>
<td>0.672</td>
<td>0.564</td>
<td>0.592</td>
<td>1.40</td>
<td>0.736</td>
</tr>
<tr>
<td>Asymp. Sig. (2-tailed)</td>
<td>0.980</td>
<td>0.148</td>
<td>0.757</td>
<td>0.908</td>
<td>0.875</td>
<td>0.128</td>
<td>0.651</td>
</tr>
</tbody>
</table>

Kolmogorov-Smirnov is a goodness of fit test used to determine if a given sample of data came from some known family of distributions. One of the suppositions of linear Regression analysis is normality. Therefore, to test if the sample data came from a normal population, Kolmogorov-Smirnov test is used to test the void hypothesis that the data came from a
normally distributed population. The null hypothesis is rejected if the p value is more than the specified level of significance (0.05). In this research the null hypothesis is not discarded for all the variables implying all the sample came from a normal distribution.

4.3.1.2 Heteroskedasticity Test Using Glejser

Table 4.9 HETEROSEDASTICITY TABLE

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.000</td>
<td>5</td>
<td>.000</td>
<td>4.258</td>
<td>.093b</td>
</tr>
<tr>
<td>1 Residual</td>
<td>.000</td>
<td>4</td>
<td>.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>.000</td>
<td>9</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: AbsUt
b. Predictors: (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH
Source: Authors’ compilation, generated using SPSS 2017

Heteroskedasticity exists in an exceedingly model if the alterations of the error-term of the various observations don't seem to be an equivalent (Gujrati, 2004). Further; a test for heteroscedasticity was conducted using the Glejser test. This was done to establish whether the variance of the error terms was constant. The effect of this is that when the error terms don’t have constant variances, the results of the model may be inefficient and estimates may be biased. The results are indicated in Table 9. Based on output coefficient the obtained value of sig. (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH 0.93 meaning that the value of the variables (Constant), LEVERAGE, TANGIBILITY, SIZE, AGE OF THE FIRM, GROWTH > 0.05, it can be concluded that there is no heteroskedasticity problem.
4.3.1.3 Multicollinearity Test

Multicollinearity denotes to a state of affairs with a high association midst the informative variables within a various correlation model or is that the absence of freedom among the informative variables during a data set. The researcher used Variance Inflation factor (VIF) to check multiple correlation that refers to actual disparity share to total disparity. More than 10 for VIF values indicate high degrees of multiple correlations among the independent variables (Hair, Babin, Anderson and Talham 2006). The tables show the results

Table 4.10: ROA TABLE OF MULTICOLLINEARITY

<table>
<thead>
<tr>
<th>Model</th>
<th>Collinearity Statistics</th>
<th>Tolerance</th>
<th>VIF</th>
</tr>
</thead>
<tbody>
<tr>
<td>AGE OF THE FIRM</td>
<td></td>
<td>.161</td>
<td>6.230</td>
</tr>
<tr>
<td>SIZE</td>
<td></td>
<td>.047</td>
<td>21.294</td>
</tr>
<tr>
<td>TANGIBILITY</td>
<td></td>
<td>.191</td>
<td>5.238</td>
</tr>
<tr>
<td>GROWTH</td>
<td></td>
<td>.027</td>
<td>37.043</td>
</tr>
<tr>
<td>LEVERAGE</td>
<td></td>
<td>.154</td>
<td>6.514</td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROA

Whenever 2 independent variables are terribly extremely related with each other, neither of them is probably going to be statistically important, albeit they will each be extremely correlative with the dependent variable. The partial regression coefficients for each of those independent variables can have comparatively massive standard errors exactly as a result of they're extremely correlative with each other. High correlations among predictor variables might indicate multiple correlations; however it isn’t a reliable indicator that it exists. It
doesn't essentially indicate a tangle. However high is just too high depends on the sample size as the sample gets larger higher correlations are tolerable. Likewise, multiple correlations will exist while not a high correlation among predictors. 2 common examples are redundant info in summed variables or between increasing terms (quadratics and polynomials) and the variables that build them up.

Table 4.11: ROE TABLE OF MULTICOLLINEARITY

<table>
<thead>
<tr>
<th>Model</th>
<th>Collinearity Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Tolerance</td>
</tr>
<tr>
<td>AGE OF THE FIRM</td>
<td>.161</td>
</tr>
<tr>
<td>SIZE</td>
<td>.047</td>
</tr>
<tr>
<td>TANGIBILITY</td>
<td>.191</td>
</tr>
<tr>
<td>GROWTH</td>
<td>.027</td>
</tr>
<tr>
<td>LEVERAGE</td>
<td>.154</td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROE

Source: Authors’ compilation, generated using SPSS 2017

The results above show that FIRM AGE, TANGIBILITY AND LEVERAGE have a moderate level of Multicollinearity in the table while SIZE and GROWTH have a high level of multicollinearity, which means that one will be linearly foretold from the others with a contrivable degree of precision. During this state of affairs the constant estimations of the multiple regressions could amendment unpredictably in retort to little vagaries within the model or the info. Collinearity doesn't cut back the prognostic power or dependability of the model as a whole, a minimum of within the sample data themselves; it solely affects calculations concerning individual predictors. This can be clarified by the point that size has an indirect effect on the firm growth.
CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This section confers the précis of the leads to section four. Finale and commendation drained from these discoveries are conversed in affiliation to the goals of the study that was to inaugurate the impact of capital structure on financial performance of Islamic banks of Kenya.

5.2 Summary of Findings

The outlines of the findings are conferred in this chapter. The intention of the study was to look at the connection flanked by capital structure and financial performance of the Islamic banks of Kenya. The study gave objective answers to the subsequent analysis questions: what's the connection between the size and financial performance of Islamic banks in Kenya? What’s the eventuality of age of a firm on the financial performance of Kenyan Islamic banks? What’s the bond between the firm’s asset tangibility and financial performance of the Kenyan Islamic banks? What’s the relation of the banks growth opportunity and financial performance of the Kenyan Islamic banks? What’s the connection betwixt financial leverage and financial performance of the Kenyan Islamic banks?

Capital structure calls are the foremost vital selections to be used in any concern for boosting of shareholders wealth and continual growth. This study was restricted to the eventuality of capital structure on the financial performance within the milieu of Kenyan Islamic banks. A panel data regression for 2 Islamic banks in Kenya throughout the period
2011 to 2015 was used. This project examined through empirical observation the repercussion of concept of capital structure in Kenya Islamic banks. The outcomes of multivariate analysis unveil that size of the firm, age of the firm, asset tangibility, growth opportunities and financial leverage as independent variable while the financial performance (ROA) and (ROE) are dependent variables. The finding of the analysis is supporting Modigliani & Miller proposition in 1958, pecking order theory, trade-off theory and agency cost theory. From the analysis in Chapter Four, it may be determined that capital structure has some effect on financial performance of Islamic banks in Kenya.

5.2.1 Size of the firm

The consequences spectacle that SIZE has a constructive and momentous consequence on financial performance; that is on ROA alone but when it comes to ROE it didn’t show any significance value. This study sustained by trade-off theory, it explicit that size mirrors larger variation, competitive advantage over small firms’, larger entree to new expertise and economical springs of funds. Tarawneh (2006) postulates that the banks doesn't perpetually means has healthier profit if or when they have tall total capital, assets performance, credits, or total deposits but working potency and asset running, absolutely inspirited the financial performance of those banks. Forasmuch as his experimental study he ended that the operative potency and asset controlling, additionally to the bank size, powerfully and absolutely swayed financial performance of the banks.

5.2.2 Age of the firm

Both in table 4 and 7 in chapter four the outcome of multiple regression showed that age has a deleterious and substantial result on the financial performance that in both ROA and ROE.
The study also proves that there is inverse liaison linking the two variables. Abdullah, Ismail, Uli & Che Rose (2010), firms that are old in the line of business perform better than the firms which are fresh. This is because as times goes by, the hazard rate descends with time and firm survival in the setting increases with the firm existence in the setting (Person, 2004). This is also reflected in Dogan (2013) study from 2008 to 2011 which spotlighted on 200 corporations registered on the Istanbul Stock Exchange. The study established a depressing association involving profitability and age.

5.2.3 Asset Tangibility

Similarly, the results also show that TANG, p-value is significant and has an undesirable and momentous influence on the financial performance. This is against the theoretical expectations. This denotes that the sampled of Kenyan Islamic banks weren't proficient to develop the illiquid asset masterpiece of their total assets fairly to influence utterly on their performance.

5.2.4 Growth opportunity

For each measures of financial performance that's ROA and ROE the regression outcome displays an optimistic affiliation between a firm's growth opportunities and performance of the firm. This is often supported by, if companies discern that they're economical, they develop and live on. If not if companies that acquire systematically an undesirable info they drop and ultimately vacate the market (Bhattacharjee, 2005).
5.2.5 Financial leverage

There was no significance in ROA nor ROE since findings concluded that financial leverage didn't back to financial performance of the companies. This is an indication that for Islamic banks in Kenya there is a rebuff noteworthy effect on their financial performance in whichever way they finance their capital pie.

5.3 Conclusions of the study

It was established that size of the bank is constructive and considerably associated with financial performance and therefore it absolutely was concluded that the scale of the bank will have a major result on the financial performance of the Islamic banks in Kenya. The importance of size of the firm on performance designates the massive corporations will net high returns paralleled to minor corporations, possibly as results of broadening of venture and economy of scale. Therefore, it's key for a corporation to be giant so as to own grander performance.

Secondly, it was concluded that age of the bank negatively affects the financial performance of a company. As a result an escalation in the age of the Islamic banks in Kenya would result in a reduction in the financial performance of Islamic banks in Kenya. Thirdly, asset tangibility affects the company’s financial performance negatively and thus an increase in the asset tangibility of Islamic banks in Kenya would result in a reduced financial performance whereas a reduction in the asset tangibility levels of the company would lead to an increased financial performance of Islamic banks in Kenya.
Fourthly, growth chance features an affirmative link amid a capital structure and financial performance of the Islamic banks in Kenya. The positive relationship may well be one amongst the simplest choices for the firm, as a result of the investors and shareholders like investment in profitable projects. In conclusion on financial leverage there's no significance of this variable since no impact was obtained between capital structures on the financial performance of Islamic banks in Kenya. Typically it will so be ended that capital structure do have a robust positive relationship with financial performance of Islamic banks in Kenya and also the impact is big and thus vital. So it also can be concluded that these variables above are among major factors of capital structure that have an effect on the performance of Islamic banks in Kenya.

5.4 Recommendations of the study

An Islamic monetary system can take part in a very imperative role in economic progress of Islamic countries plus non-Islamic countries by drumming up quiescent reserves that are in the vicinity and globally restrained of interest based financially conduits and assisting progress of capital souks. The upshots of this study have substantial policy insinuations at the business, industry segment and abstract levels. The study proposes these recommendations to the IBs

First and foremost, IBs are suggested to fastidiously choose the suitable and cost-effective apportionment of their treasuries. IBs ought to meticulously screen their endowment utilization in Musharaka, Ijara, Murabaha, Mudaraba and different Islamic financial
instruments and punctiliously opt for their credit distribution within the utmost gainful venture with a tolerable peril. Secondly, because of the Islamic banking guideline, they aren't allowable to implicate in high risk undertakings; thus, IBs will raise their total asset by swelling the credit to clientele. So as to extend the loan to clients, the bank will escalate the deposit from clients by giving hibah (gift in business banks) to lure in account holders, this will initial increase the deposit of the customers, thus an excess fund to form loan and alternative financial activities. IBs will surge their asset by giving lesser riba (interest rate in business banks) to draw in a lot of customers to borrow. Thirdly, the study further revealed that offering high financial returns for depositors could be a solution to increase the growth opportunity experienced. The study recommends that the banks should be keen in providing Sharia compliant solutions that are meant to seal the breach that subsists in the convectional banks. Islamic banks should continually innovate to offer new products that meet the customer needs and also to keep up with competition in the market place.

In addition to that the IBs will increase the availability of a broad vary of personal capital funding across all stages of finance by collaborating with the Gov’t and alternative agencies. They will conjointly strengthen institutional arrangements to produce financial services to the underserved and build capability of practitioners to support this in a good and sustainable manner. Excluding this when it involves the market; they need completely different choices like they will promote an efficient and competitive money market with bigger depth and liquidity and additionally promote active participation in supplying and commercialism of sukuk that's Issue equity participation notes by the Gov’t and government-linked firms for project funding. Last however not least the IBs will strengthen
the institutional structure of financial institutions to produce adequate safeguards against contagion risk and excessive leverage

### 5.6 Suggestion for further research

This study could be a groundbreaking for coming analysis in this area, notably in Kenya. First, this study centralized on capital structures variables beneath study and their effect on financial performance of the Islamic financial institutions and thus, simplification cannot adequately broaden to alternative sectors. In consequence, further analysis got to be distributed to outline alternative causes that have an effect on financial performance. Aspects like managerial ability, capitalization of the firm, intangible assets are counseled for future study. On the alternative hand other measures of financial performance are often used, like operative margin of profit and return on capital employed.

Finally, this study was based in two Islamic banks which they have only been in the market for hardly ten years. The same study should be carried out to cover a larger geographic region that would provide a fair representation and longer periods and select more established Islamic banks.
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*Development Group*, university of Ontario, Institute of technology, Ontario 40-54


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APPENDICES

APPENDIX I: INTRODUCTORY LETTER

KENYATTA UNIVERSITY
GRADUATE SCHOOL

E-mail: dean-graduate@ku.ac.ke
Website: www.ku.ac.ke

P.O. Box 43844, 00100
NAIROBI, KENYA
Tel. 8710901 Ext. 57530

Our Ref: D53/MSA/PT/33160/2014

DATE: 30th January, 2017

Director General,
National Commission for Science, Technology
and Innovation
P.O. Box 30623-00100
NAIROBI

Dear Sir/Madam,

D53/MSA/PT/33160/2014.

I write to introduce Mr. Ahmed Shariff Salim who is a Postgraduate Student of this University.
He is registered for M.B.A degree programme in the Department of Accounting and Finance.

Mr. Ahmed intends to conduct research for a M.B.A Project Proposal entitled, “Capital
Structure and Financial Performance of Islamic Banks in Kenya”.

Any assistance given will be highly appreciated.

Yours faithfully,

[Signature]

MRS. LUCY N. MBAABU
FOR: DEAN, GRADUATE SCHOOL

AM/Ibn
APPENDIX II: PERMISSION LETTER FROM NACOSTI

NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY AND INNOVATION

Telephone: 020 400 7001,
0713 788787, 0735404245
Fax: +254-20-318245, 318249
Email: dgt@nacosti.go.ke
Website: www.nacosti.go.ke
When replying please quote

Ref: No. NACOSTI/P/18/95876/22305

Date: 25th April, 2018

Salim Shariff Ahmed
Kenyatta University
P.O Box: 43844-00100
NAIROBI.

RE: RESEARCH AUTHORIZATION

Following your application for authority to carry out research on “Capital structure and financial performance of Islamic Banks in Kenya” I am pleased to inform you that you have been authorized to undertake research in Mombasa County for the period ending 23rd April, 2019.

You are advised to report to the County Commissioner and the County Director of Education, Mombasa County before embarking on the research project.

Kindly note that, as an applicant who has been licensed under the Science, Technology and Innovation Act, 2013 to conduct research in Kenya, you shall deposit a copy of the final research report to the Commission within one year of completion. The soft copy of the same should be submitted through the Online Research Information System.

[Signature]
DR. STEPHEN K. KIBIRU, PhD.
FOR: DIRECTOR-GENERAL/CEO

Copy to:

The County Commissioner
Mombasa County.

The County Director of Education
Mombasa County.
APPENDIX III: AUTHORIZATION LETTER FROM COUNTY COMMISSIONER AND COUNTY DIRECTOR OF EDUCATION

THE PRESIDENCY
MINISTRY OF INTERIOR AND COORDINATION OF NATIONAL GOVERNMENT

Telephone: Mombasa 2311201
Tel. 0715 040444
Email: mombasacountycommissioner@yahoo.com
When Replying please quote:

Ref. no. MCC/ADM.25 VOL.1/162 3rd May, 2018

Deputy County Commissioners
MOMBASA COUNTY

RE: RESEARCH AUTHORIZATION – SALIM SHARIFF AHMED
PERMIT NO. NACOSTI/P/18/95876/22305

This is to authorize the above named student from Kenyatta University, Nairobi to carry out research on “Capital Structure and financial performance of Islamic Banks in Kenya ” in Mombasa County for the period ending 23rd April, 2019.

Any assistance accorded to him will be highly appreciated.

RASHID WERE
FOR: COUNTY COMMISSIONER
MOMBASA COUNTY

C.C.

County Director of Education
MOMBASA
APPENDIX IV: REGISTERED ISLAMIC FINANCE INSTITUTIONS IN KENYA

1. First Community Bank Limited

2. Gulf African Bank Limited

Source: Central Bank of Kenya, 2016
APPENDIX V: DATA COLLECTION SCHEDULE

DATA COLLECTION GUIDE

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