

## **Abstract**

Wide interest margins as witnessed in Kenya are a sign of a repressed and inefficient financial sector. This paper carries out a cross-country analysis of the determinants of financial market efficiency using panel cointegration with a view to recommending policy options for improving the efficiency of the financial sector intermediation process in Kenya. The study finds that the major contributors to the differences in financial sector inefficiency in Kenya compared to the other countries in the study are high bank operating costs, default risk and financial market structure. The study recommends, among other measures, that the government through the Central Bank need to collaborate with the commercial banks and establish a working credit reference bureau to enable easy identification of credit worthy customers in order to reduce default risk; there is also need by the central bank to license more new banks to increase competition and reduce bank concentration. The study also recommends increased use of technology including phone-banking and e-banking to reduce operation costs of the banks. The paper concludes that contrary to the findings from other cross-country analysis, the factors that lead to financial market in/efficiency varies from one country to the other.