

**POLITICAL RISK, CREDIT RISK MANAGEMENT AND LIQUIDITY OF
COMMERCIAL BANKS IN KENYA**

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AND TOURISM IN PARTIAL FULFILMENT FOR THE AWARD OF A DEGREE OF
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DECLARATION

This research project is my original work that has never been presented for an award of a degree in any other University

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DEDICATION

To my sister Marian, I am grateful for the support in terms of printing. Allah bless you

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ABBREVIATIONS AND ACRONYMS

CBK	Central Bank of Kenya
CRB	Credit Reference Bureau
CRM	Credit Risk Management
DTA	Deposits to Asset
GDP	Gross Domestic Product
ICRG	International Country Risk Guide
LTA	Loan to Assets
LTD	Loan to Deposit
MENA	Middle East and North Africa
MPT	Modern Portfolio Theory
NACOSTI	National Commission of Science, Technology and Innovation
NPLs	Non-Performing Loans
SACCOs	Savings and Credit Cooperatives Organizations
SMEs	Small and Medium Enterprises

OPERATIONAL DEFINITION OF TERMS

Credit information sharing	A continuous process that occurs among existing financial institutions and the licensed credit referencing bureaus. In this study it was measured through credit scores, reports and credit history
Credit risk management	It is a continuous process that aims at reducing possibility of loan default by customers of the bank represented in this study by timely credit information sharing, adequate loan loss provisioning and having in place correct lending requirements to reduce non-performing loans of banks. In this study, this variable was measured by credit information sharing, loan loss provisioning as well as lending requirements
Lending requirements	The conditions that borrowers must fulfil to qualify for a credit facility. It was measured in this study by identification requirement, logbooks and tittle deeds in their possession and ownership
Liquidity	The ability of the bank to meet its short-term obligation using current assets and it was measured in this study by ratio of total loans to total deposits
Loan loss provisioning	The amount of funds set aside to cushion the bank from non-performing loans and it was measured in this study using the ratio of total loan provision against total loans
Political risk	The probability of loss of returns from investments as a result of unforeseen political events and it was measured in this study by the political risk index

ABSTRACT

Liquidity has remained a challenge among commercial banks in Kenya. For instance, the ratio of loans against deposits of the said banks stood at 0.740969, 0.74092, 1, 0.713654 and 0.795822 with an average value being 0.798273 across the period 2018, 2019, 2020, 2021 and 2022 respectively. This implies that most of the commercial banks did not have adequate assets as compared to deposits needed to finance customer loan requests which provide evidence of liquidity concerns among commercial banks in Kenya. Commercial banks can play an important role in the economy of developing countries like Kenya through their financial intermediation role, supporting borrowing and investment and hence economic growth. However, the aforementioned concerns imply that Kenya is yet to enjoy the significant role of a banking sector. Thus, this study sought to establish the effect of credit risk management on liquidity of commercial banks in Kenya. More specifically, the link between credit information sharing, loan loss provisioning and lending requirements and liquidity of commercial banks in Kenya with political risk as a moderator variable was considered in this study. The study was guided by the information asymmetry, transaction cost, the modern portfolio theory and liquidity preference theory. Positivist research philosophy was adopted in this study besides explanatory design. The study targeted 39 Kenyan banks and census was used. Information was collected from primary sources on information sharing and lending requirements while secondary data on a period 2018-2022 was gathered on loan loss provisioning and liquidity. The questionnaire was pilot tested before data gathering process among 4 credit managers from commercial banks in Kenya. The reason for pilot testing was to determine reliability of questionnaire while its validity was ensured by supervisor and two experts in the field of finance. Processing of the gathered data was done descriptively and inferentially and presented in tabular and graphical forms. Multicollinearity, normality was conducted as diagnostic tests before regression analysis to test its assumptions. The ethical issues that were considered in this study included appropriate citation and referencing of the information reviewed to avoid plagiarism and voluntary participation by respondents. The findings were that credit information sharing ($p < 0.05$), loan loss provisioning ($p < 0.05$) and lending requirements ($p < 0.05$) had significant effect on liquidity of commercial banks as moderated by political risk ($p < 0.05$). The study concluded that credit risk management and liquidity of commercial banks in Kenya are significantly related with each other with political risk as a moderator variable. It was recommended that Credit Managers working among commercial banks in Kenya should invest in latest technologies for carrying out timely credit information of customers with the licensed Reference Bureaus. The loan officers working with commercial banks in Kenya should diversify into loan portfolio in order to remain stable and have meaningful contribution to the growth of an economy. Managers working with commercial banks in Kenya should effectively invest in lending requirements like land title deeds and logbooks in order to improve on their credit risk management which in turn can allow them achieve optimal and required liquidity levels. The government of Kenya should seek to improve on the existing political environment in the country so as to positively influence liquidity level and thus promoting financial stability of the commercial banks.

CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Liquidity is an important construct that is of great concern to policy makers and regulators (World Bank, 2023). By nature, commercial banks are required to maintain adequate liquidity so as to finance short term by depositors (IMF, 2023). Adequate liquidity is sufficient predictor of financial stability of commercial banks at large (Chodorow-Reich, Darmouni, Luck & Plosser, 2022). However, too much liquidity may represent tied up capital that could have otherwise been used to finance projects which would maximize the wealth of shareholders of the institution. Balancing liquidity positions implies that commercial banks should strike equilibrium between its current assets and liabilities (Ali, Shah & Chughtai, 2019).

The lending operations and information asymmetry between lenders and borrowers are key forces that increase credit risk among commercial banks. Information asymmetry creates moral hazard and adverse selection that in turn pose challenges for lenders to effectively appraise borrowers during loan application process (Chen, Chen & Huang, 2021). All these forces contribute towards credit risk among commercial banks. Since lending is the major activities undertaken by financial institution like commercial banks, credit risk from these activities is the most pronounced risk exposure by these institutions (Orichom & Omeke, 2021). However, as observed by Li (2019), too much exposure to credit risk can threaten overall liquidity position and thus stability of commercial banks.

Political risk is the chance that a nation's political unrest or developments could negatively impact the firm. There is a growing body of literature focusing on political risk as a moderator variable

(Behera, Behera & Sethi, 2024), its effect on the relationship between credit risk management and liquidity in the financial sector has remained largely unexplored.

Liquidity of commercial banks in developed countries has attracted significant scholarly attention. In United States for instance, Adrian, Abbas, Ramirez and Dionis (2024) argue that the banking sector has been marked with liquidity concerns, demonstrated by collapse of major institutions like Silicon Valley Bank (SVB), Signature Bank (SBNY) and First Republic Bank (FRB) respectively. This liquidity challenge faced by commercial banks in USA can be attributed to ineffective credit risk management practices among some institutions (Adrian et al., 2024). For China, liquidity of the banking sector is characterised by weakened deposit base (Hou, 2024). Borrowing evidence from Ukraine, Cai and Zhang (2017) documented that banks with high exposure to credit risk as demonstrated by an increase in non-performing loans (NPLs) may face liquidity constraints making it hard for them to meet the withdrawal demands of depositors. Among commercial banks in Europe, Golubeva, Duljic and Keminen (2019) were of the view that liquidity and thus profitability of a bank increases with an improvement in liquidity risk management endeavor of the financial institution.

Evidence from Middle East and North Africa (MENA) region by Ghenimi, Chaibi and Omri (2017) indicate that credit risk and liquidity in the context of financial institution are significantly linked with each other. Related evidence in MENA region indicates that liquidity risk negatively affects liquidity and thus profitability position of a bank (Abdelaziz, Rim & Helmi, 2022). In Nigeria, Ayinuola and Gumel (2023) indicated that credit risk has negative implication on financial stability and thus liquidity position of commercial banks.

Just like the rest of the world, commercial banks in Uganda are also marred with liquidity problems. According to Musiita, Boyi, Kisaalita, Mutungi and Mbabazize (2023), liquidity position of

commercial banks in Uganda has been on a declining trend falling short of the Bank of Uganda's cut-off point of 20% of liquid assets to total deposits liabilities. Liquidity problems are highly pronounced among commercial banks in Rwanda. According to Namata (2022), there was liquidity constraint among commercial banks in Rwanda in the first half of 2022, resulting into restricted access to credit. This trend was attributed to reduced deposits and an increase in lending to the private sector in the economy. In spite of the growing concern of liquidity of commercial banks, its nexus with credit risk management has not received adequate scholarly attention.

Liquidity challenges encountered by commercial banks in other regions are not unique from those in Kenya. According to Waweru and Oribu (2023), some banks in Kenya have been characterised by liquidity challenges such as Development Bank of Kenya, Consolidated Bank as well as National Bank and Housing Finance Corporation with some of these institutions reporting negative liquidity positions against required threshold. According to Kiemo, Talam and Rugiri (2022), some banks in Kenya are characterised by higher credit risks demonstrated by greater non-performing loans against gross loans creative vulnerability in the banking sector. This trend is also a big threat to overall financial stability of the banking sector in Kenya. According to Karanja (2025), the financial intermediation role of commercial banks expose commercial banks to diverse risks, key one being credit risk. This underscores the need for effective credit risk management to allow commercial banks effectively play their financial intermediation role in economy of Kenya.

1.1.1 Liquidity of Commercial Banks

In a lending institution like a commercial bank, such short-term obligations including customer borrowing and creditors (Ghenimi, Chaibi & Omri, 2017). Low liquidity position of the financial institution may signal possibility of financial distress (Li, 2019). Persistent financial distress concerns may in turn transform into insolvency and possible bankruptcy proceeding of a financial

institution (Waweru & Oribu, 2023). Regulators are more interested in the liquidity position of commercial banks since liquidity constraints of these institutions and possible financial distress may put the deposits of customers at greater risk. On this account therefore, liquidity is an important parameter and particularly in lending institutions like commercial banks (Golubeva, Duljic & Keminen, 2019).

In the context of commercial banks, liquidity is measured through different indicators; these include current assets against current liability, deposits to asset (DTA) ratio, loan to deposit (LTD) ratio and loan to asset (LTA) ratio (Chen, Chen & Huang, 2021). DTA ratio is used to provide measurement of how assets of the bank can be used to finance deposits. LTD ratio indicates how the financial institutional leverages its deposits to fund loans. LTA ratio represents the adequacy of the assets of the bank to finance loans demanded by customers (Abuga, Wamugo & Makori, 2023). The present study measured liquidity using LTD and Figure 1.1 gives a comprehensive analysis of liquidity position of the whole 39 commercial banks combined. LTD was adopted as a proxy of liquidity.

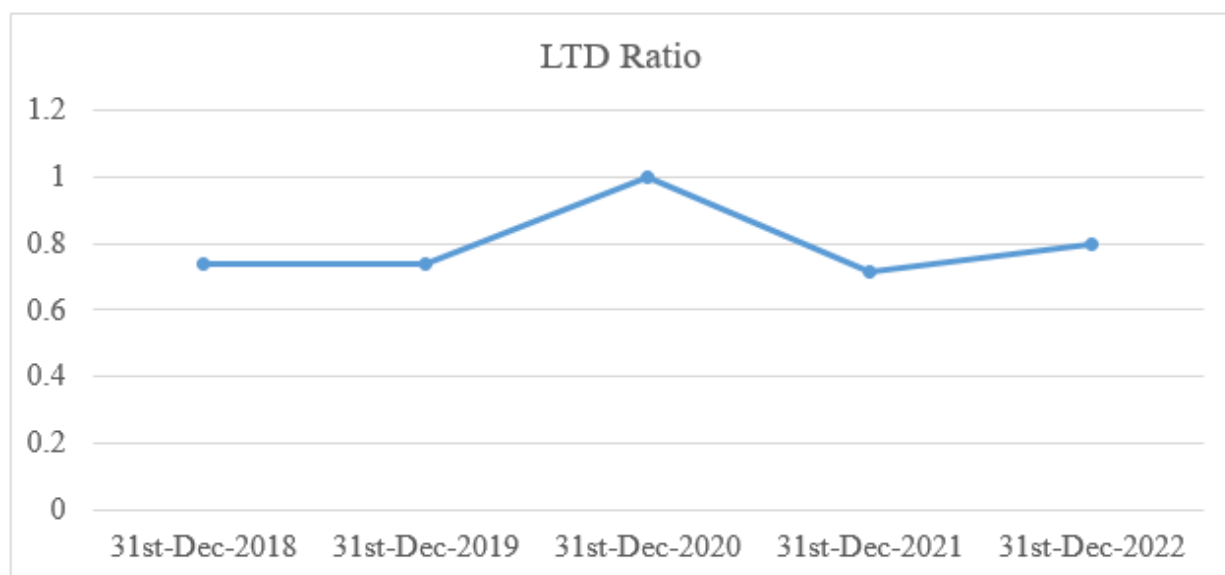


Figure 1.1: Loan to Deposit Ratio Analysis of Commercial Banks in Kenya

Source: CBK Reports (2022)

Figure 1.1 shows that liquidity position of Kenyan banks on the basis of LTD ration (loans/deposit) stood at 0.740969, 0.74092, 1, 0.713654 and 0.795822 with an average value being 0.798273 across the period 2018, 2019, 2020, 2021 and 2022 respectively. Hence, the findings in Figure 1.1 critically show that as commercial banks in Kenya were doing relatively better in terms LTD. This implies that commercial banks relied more on deposits from customers to finance loans as compared to assets. This could possibly imply that more deposits and fewer assets were in place among commercial banks to fund deposit that signaling liquidity issues. In this study, liquidity was measured by loan to deposit ratio.

1.1.2 Credit Risk Management

Credit risk management is an effective processing that seeks to enhance timely credit information sharing, adequate loan loss provisioning and having in place correct lending requirements to reduce non-performing loans of banks (Saiz-Sepúlveda & Hernández-Tamurejo, 2025). Credit risk arises when borrowers are not in position to pay the advanced loan facilities on time as specified in terms of the contract (Ekinci & Poyraz, 2019). It is defined as the inability of the borrower to service the interests and principal amount of loan on time (Cai & Zhang, 2017). Credit risk management on the other hand is a set of practices that are embraced by the financial institution limit exposure to poor loan quality (Orichom & Omeke, 2021). CRM can be achieved through credit information sharing, loan loss provisioning and lending requirements (Cai & Zhang, 2017). Siddique, Khan and Khan (2021) indicated that credit risk management can be measured through capital adequacy and cost efficiency ratio. The measures of credit risk management adopted by Owing's (2017) include loan loss provisioning, capital adequacy and NPL ratio. Kabugu and

Wamiori (2022) used credit referencing and collateral requirement as measures of credit risk management. Olobo, Karyeija, Sande and Khoch (2021) used credit risk identification, assessment and control as measures of credit risk management. This study adopted credit information sharing, loan loss provisioning and lending requirements as the key measures of credit risk management.

Credit information sharing is done at the initial stage of customer appraisal process where information on credit history of borrowers is obtained from the Credit Reference Bureau (CRB) to make the decision on lending (Asongu, Kayo, Tchamyou & Zogo, 2025). Thus, credit information sharing eases the process of loan application process (Van-Greuning & Bratanovic, 2020). Credit information sharing provide mechanisms where lenders have an opportunity of assessing borrowers reports from the Credit Reference Bureaus that provides more information on repayment patterns of customers (Bowen & Makokha, 2021). In Kenya for instance, some of the CRBs include Metropol as well as TranzUnion among others and they provide such services as the credit scores, credit reports and credit histories as well as the clearance certificates for the defaulted clients. These institutions play an instrumental role in determining the credit worthiness of the borrowers (Mungiria & Ondabu, 2019).

Loan loss provisioning is setting of an expense in the income statement of the financial institution that cushions the uncollected loans and payments (Danisman, Demir & Ozili, 2021). In order to present an accurate picture of the financial status, commercial banks are mandated to provide an account of all expenses and loan defaults hence the need for loan loss provisioning in the financial statements (Nugroho, Arif & Halik, 2021). Loan loss provision is basically an expense in the income statement that is set aside as a way of providing an opportunity for allowing the uncollected loans and for payment of loans (Lai & Goh, 2025). Loan loss provision obligates commercial banks to ensure all potential loan defaults and related expenses have been accounted for (Nugroho,

Arif & Halik, 2021). The widely available and documented measures of loan loss provisioning include loan loss provision and gross loans (Okeyo, Odoyo & Omboi, 2023) as well as the ratio of total loan provision against total loans (Ozili & Outa, 2017).

Lending requirements are specific documents that borrowers are required to submit to lenders to support their loan appraisal process. These requirements include the national identity cards, official pay-slips and log books or land title deeds among others (Fraisie, Lé&Thesmar, 2020). Other common lending requirements that commercial banks require from borrowers during the loan appraisal process include their identification requirements like the passports, their levels of income and the amount of their collaterals (Golubeva, Duljic & Keminen, 2019).

1.1.3 Political Risk

Political risk arises when investors in a country have fear of losing their money or making lower returns from their invested as expected as a result of the prevailing political conditions, decisions or events in the country. Political risk is a major concern for investors in a country and in governments where this is not considered, a high price of investment loss is paid. Studies leveraging political risk as a moderator variable include Mokaya, Jagongo, James and Ouma (2018). Molonko and Ampah (2018) suggested that political risk is a significant moderator variable. Based on the empirical evidence, political risk was considered as a moderator variable in this proposed study.

The measures of political risk include the political risk index which the information that can easily be accessed from the statistics of the World Bank reports (Kirikkaleli, 2020). The other measures of political risk include the ICRG's Political risk Ratings as well as the use of dummy variables (Banerjee & Dutta, 2022). While the use of information from Word Bank and ICRG to determine the political index can generally be regarded as quantitative based on a number of variables that

weigh an aggregate score, the use of dummy variables as measures of political risk is more qualitative (Şanlısoy, Aydın, Yalçınkaya & Elif, 2017).

1.1.4 Commercial Banks in Kenya

These are institutions established to mobilize deposits from customers which are then used as capital to finance loan applications by customers (Abuga, Wamugo & Makori, 2023). These institutions are regarded as financial intermediaries since they link borrowers and depositors resulting into financial intermediation process (Otiende, 2021). The implication of the said financial intermediation process to the long-term growth of an economy cannot be underscored since the same supports savings and investments as well as capital creation. Besides achieving financial intermediation, commercial banks also contribute towards financial inclusion in an economy (Abuga, Wamugo & Makori, 2023).

Kenyan banks are classified into three tiers based on their relative market share, customer deposits and assets. In the last 5-years, liquidity has presented the greatest challenge for most commercial banks in Kenya. There are three broad tiers of banks in Kenya, tier I, II and III (Abuga, Wamugo & Makori, 2023). These tiers are established on the basis of the assets, customer base and total deposits of the respective commercial banks in country. While tiers I and II are more stable explaining a significant proportion of their market shares with greater asset bases and customer deposits, their tier III counterparts are relatively unstable accounting of much of the liquidity issues (Malit, Scholastica & Nelson, 2023).

1.2 Statement of Problem

Banks play an integral role towards the gross domestic product of Kenya at large and in terms of facilitating financial intermediation. For instance, the contribution of Kenya's banking sector to

the entire GDP of the country in terms of their assets has always hovered around 60% for the period 2018-2022 (Malit, Scholastica & Nelson, 2023). Despite this importance, liquidity has remained a challenge among commercial banks in Kenya (Otiende, 2021). For instance, the ratio of loans against deposits (LTD) of the said banks stood at 0.740969, 0.74092, 1, 0.713654 and 0.795822 with an average value being 0.798273 across the period 2018, 2019, 2020, 2021 and 2022 respectively (CBK, 2022). This implies that most of the commercial banks did not have adequate assets as compared to deposits needed to finance customer loan requests which provide evidence of liquidity concerns among commercial banks in Kenya. Although CBK has played an instrumental role in ensuring that commercial banks in Kenya are well capitalized and that corporate governance mechanisms are strengthened to safeguard their stability, it remains unclear if all these efforts have materialized (Abuga, Wamugo & Makori, 2023). Thus, urgent measures need to be undertaken to improve liquidity position of commercial banks in Kenya failure to which possible financial distress and ultimate bankruptcy is inherent and depositors would lose significant amount of their deposits.

Some of the existing studies create contextual gaps by focusing on Ukraine (Cai & Zhang 2017) and Nigeria (Ayinuola and Gumel, 2023) underscoring the need for similar studies in Kenya. Local studies including Gumel (2023) and Ghenimiet *al.* (2017) focused on financial stability as the dependent variable and not liquidity and thus creating conceptual gap. According to Waweru and Oribu (2023), liquidity is more critical to a financial institution like commercial banks that require adequate cash to fund loan requests so as to achieve financial liquidity. This assertion was buttressed by Golubeva, Duljic and Keminin (2019) who indicated that regulators like central banks are keener to ensure commercial banks are more liquid in order to achieve financial stability. Thus, the empirical evidence linking credit risk and specifically liquidity in the context of

commercial banks in Kenya is scanty. Similarly, the role played by political risk in credit risk and liquidity interactions both from global, regional and local perspectives has not received adequate attention thus the need of carrying out the present study. Hence, against these gaps, the present study sought to establish the effect of credit risk management on liquidity of commercial banks in Kenya.

1.3 Objectives of the Study

1.3.1 General Objective

The general objective of the study is to establish the effect of credit risk management on liquidity of commercial banks in Kenya.

1.3.2 Specific Objectives

The study was guided by the following specific objectives:

- i. To determine the effect of credit information sharing on liquidity of commercial banks in Kenya.
- ii. To establish the effect of loan loss provisioning on liquidity of commercial in Nairobi Kenya.
- iii. To examine the effect of lending requirements on liquidity of commercial banks in Kenya.
- iv. To find out the moderating effect of the political risk on the relationship between credit risk management on liquidity of commercial banks in Kenya.

1.4 Research Hypotheses

The study sought to test the following hypotheses:

H0₁: Credit information sharing has no significant effect on liquidity of commercial banks in Nairobi Kenya.

H0₂: Loan loss provisioning has no significant effect on liquidity of commercial banks in Nairobi Kenya.

H0₃: Lending requirements have no significant effect on liquidity of commercial banks in Nairobi Kenya.

H0₄: Political risk has no significant moderating effect on the relationship between credit risk management on liquidity of commercial banks in Nairobi Kenya.

1.5 Significance of the Study

Credit and loan officers and managers working among commercial banks in Kenya would benefit from this study by understanding informed credit risk management practices. The study would guide these professional during their credit risk appraisal and analysis so that informed lending decisions are made. The study would inform new policies among commercial banks in Kenya to guide credit risk management undertakings conducted on a daily basis. Shareholders of commercial banks may benefit from this study by gaining insights on how to enhance liquidity of their institutions to allow them maximize their wealth.

Policy makers at CBK would be guided in their policy credit risk policy formulation endeavors. Policy makers working at Kenya Bankers Association KBA may rely on the findings of this study to formulate policies that would enhance liquidity of their respective member banks. The study would contribute to overall knowledge and information available linking credit risk management and liquidity. Future scholars and academicians carrying out related studies may use this study as

a reference point, to increase the available body of literature linking credit risk management and liquidity.

1.6 Scope of the Study

The nexus between credit risk, political risk and liquidity was explored in the proposed study. While credit risk management and liquidity were independent and dependent variables respectively, political risk was studied as a moderator variable. The specific aspects of credit risk management covered included credit information sharing, loan loss provisioning and lending requirements. The study covered the period of years (2018-2022). This period was selected by this study because significant developments in the banking sector like heavy investment in new technologies as well as the mass of COVID-19 also reached peak within the same period and it was interesting to establish if these issues led to liquidity concerns in the banking sectors aside credit risk management. The study collected both primary and secondary data and hence mixed approach was adopted. The analysis was supported by means and standard deviations as well as multiple regression analysis.

1.7 Limitations of the Study

Some of the participants during data gathering exercise were likely to be so busy with their daily schedule and this may make it hard to gather data in a single occasion. To overcome this concern, information was gathered from respondents through a drop and pick later method. Through this system, participants were given ample time to share their relevant views before the questionnaire is collected for analysis. It was anticipated that during the gathering of the information, some of the respondents would withhold very critical and sensitive information on credit risk for the fear of being victimized. In overcoming this limitation, assurance was provided to respondents that all

their information was to be held with utmost confidentiality and that it was to support the academic purpose.

1.8 Organization of the Study

Three chapters are covered in this proposal with the background of the study, research problem, objectives, hypotheses, significance and scope of the study being details of the first chapter. The review of theories, past empirical studies and knowledge gaps as well as knowledge gaps are detailed in the second chapter. The third chapter places emphasis on the methodologies that guided realization of the objectives established in the first chapter. The findings and discussions are presented in chapter four, conclusion and recommendations on the other hand are captured in chapter five.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

Literature is reviewed in this chapter covering theories and past empirical inquiries. There is also conceptual framework and a section detailing gaps from the reviewed studies.

2.2 Theoretical Review

The study was guided by the information asymmetry, transaction cost, the modern portfolio theory and liquidity preference theory.

2.2.1 Information Asymmetry Theory

The proponents of this theory include Stiglitz (1961), Akerlof (1970) and Spence (1973) and its formalization was as recent as 2001. Information asymmetry describes a situation within financial markets when there exists discrepancy in information in between lenders and the borrowers. In the interaction between these two parties, one of them has more information than the other party and the same can be used for personal gain (Chan, Siegel & Thakor, 1990). For instance, whenever the borrower has more information regarding his/her loan repayment behavior and past credit history compared to the lender, the same information can be used for personal gain which may in turn adversely affect the credit risk profile of the lending institution (Bester, 1987).

In a market that is characterized by perfection where access to information is costless by the involved parties, market failure of information may not have an adverse effect on the parties with in such markets. However, this is not true in the real and practical world where accessing information require one to incur some costs. In the real world, information is asymmetrically

distributed between lenders and borrowers. In the perspective of the lenders, such information is deemed to be incomplete (Izquierdo & Izquierdo, 2007).

This theory has undergone significant evolution from its original form, and though many economists agree that information asymmetry has consequences, there are differing views on how it affects things (Al-Hiyari, Kolsi, Lutfi & Shakkour, A2024). Information sharing can play an important role in reducing or elimination of information asymmetry that may in turn influence credit risk in the lending institution. Thus, this theory was relevant in the present study as it anchored the variable of information sharing.

2.2.2 Transaction Cost Theory

The proponent of this theory was Coase (1937) where transaction costs are classified and categorized to include are defined as the expenses that are incurred in entering negotiation agreements, monitoring as well as in enforcement of the exchanges between parties in a given transaction. The theory is underpinned on two issues: bounded rationality as well as opportunism. Bounded rationality is established on the fact that it is not possible to predict all possible contingencies related with a given situation and particularly those linked with opportunism. Hence, no contract can arise before some aspect of commitments that may cover the said contingencies. Contracts exist because of opportunism and the same cannot be abandoned (Krüger, Rösch & Scheule, 2018).

The above two conditions justify the need for transaction costs because investments and assets are specific to a given transaction. This theory over-emphasizes the central role played by asymmetrical information that arise because of some degree of dependence between a set of partners. Lending requirements are meant some of the transaction costs that financial institutions

can have in place for customers to provide correct information at the appraisal stage of the loan application process. Loan loss provisioning is also one cost that is incurred by lenders in the course of their operations which may in turn influence the credit risk of the lender (Athari & Irani, 2022).

This theory has undergone significant historical evolution and development since its formulation. Until 1980s, the development of this theory was marred with treatment of firms as entities that seek to avoid transaction costs. Since 1990s, the theory has undergone enrichment by various approaches underpinning the central role of firms in creation of positive value (Cuypers, Hennart, Silverman & Ertug, 2021). Recently, the rise of sustainable development debate has seen increased application of this theory in sustainability initiatives of firms as they seek to enhance their liquidity positions. Thus, this theory underpinned the central role that lending requirement and loan loss provisioning as far as credit risk management activities and processes of the lending are concerned among lending institutions in order to safeguard their liquidity levels and positions.

2.2.3 Modern Portfolio Theory

The proponent of this MPT was by Markowitz (1952) and it requires investors and lending institutions to diversify their loan portfolios in order to mitigate against unforeseen risky events. The theory argues that through diversification. Lenders are well positioned to minimize their exposure on risks and thus maximize the returns generated from lending operations. In this theory, diversification is viewed as the mechanism and manner in which expected returns of an enterprise including can optimally be maximized. It is theorized that asset selection for the purpose of investment should not be done individually but this should be done in reference to their prices.

It is assumed in this theory that the returns generated from operations of the firm increase with the increase in risk levels. This means that higher risks attract greater returns. Political risk is an

unforeseen event with a probability of occurrence. The occurrence of political risk may have an effect on liquidity of the lender.

Ever since its inception in early 1950s, this theory has undergone significant evolution and development, it has transformed the way financial analysts carry out their tasks. The theory has continued to shape and influence behaviour of investors as far as risk perceptions are concerned. Hence, this theory was found relevant in supporting the moderating variable political risk.

2.2.4 Liquidity Preference Theory

Keynes (1936) came up with this theory and it established three motives of why firms should hold cash as far as their operations are concerned. These motives include for transaction, precautionary or speculative purpose. The argument of this theory is that when the level of interest rate is very low, a rise in supply of money in the economy has little effect of increase in investments but only reduces the available cash balances. In the event that there is a rise in interest rate, the theory argues that people would demonstrate more willingness of holding low amount of money so that more profit is secured. Elgar (1999) indicated that people require money on the fact that he/she has an expenditure plan for financing or has some speculations on future state of interest rate or because of uncertainty concerning future.

In terms of transaction motive, money is required at an enterprise level so as to ensure that all economic transactions have been completed (Keynes, 1936). Holding cash for precautionary motive means that enterprises hold some liquid cash so that they are able to manage some emergencies that are unforeseen (Keynes, 1936). In view of speculative motive, it implies that people hold cash so that they are able to maximize opportunities arising from variation in prices

of securities and bonds in stock markets (Keynes, 1936). The present study had liquidity as its dependent variable. Thus, liquidity preference theory was used to underpin this variable.

2.3 Empirical Literature Review

Past empirical studies and gaps are identified and illustrated in the subsequent sections:

2.3.1 Credit Information Sharing and Liquidity

Hung-Son, Gia –Khanh and Thanh-Liem (2020) conducted a study on credit information sharing, corruption and financial development. The information gathered and analyzed through panel regression indicated that private credit bureaus and financial development are negatively related with each other. On the other hand, public credit registries were insignificantly linked with financial development. However, financial development and not liquidity was adopted as the dependent variable thus creating conceptual gap.

In a study conducted by Iakimenko, Semenova and Zimin (2022), the link between information sharing and credit risk was explored. Credit risk in this study was adopted and used as a proxy of bank stability. The analysis indicated an existence of a nonlinear nexus between information disclosure and credit risk. The analysis further indicated that an increase in depth of credit information disclosure decreases credit risk. This study created conceptual gap by viewing bank stability in terms of credit risk which is conceptually different from liquidity which was covered in the present study.

Bonomo, Bruschi and Schechtman (2020) carried a study on sharing of public and positive information and the implication on personal loans in Brazil. It was hypothesized that credit information sharing had potential to improve credit repayment history of the borrowers. Information was gathered with aid of primary sources as guided by the questionnaire. It was noted

after analysis that was done through ordinary least square that information asymmetry was a key factor shaping and influencing the interest rates charged by lenders. It was further evident that an increase in access to positive credit information enhances the credit market level of efficiency which in turn create benefits to timely borrowers. However, this study was conducted in Brazil that is more developed to Kenya which is still developing hence require more research like the present one to achieve liquidity and thus stability of the banking sector.

Onsarigo (2018) provided an indication that credit information sharing allowed lenders of funds to have access to reports linked with previous credit history and repayment patterns of borrowers. In this study, the effect of credit information sharing was determined through comparison between before the period after and before the bill requiring information sharing was enacted and put into practice in Kenya. The adopted design was descriptive and the analyzed findings showed that SACCOs registered greater financial performance after the credit information bill was enacted than before when the same was passed. However, the study was done among registered deposit taking SACCOs that operate under a different regulator as compared to commercial banks in Kenya hence contextual gap.

2.3.2 Loan Loss Provisioning and Liquidity

De-Araujo, Cohen and Pogliani (2021) focused on the COVID-19 pandemic and explored its implication on loan loss provisioning. The study hypothesized that this pandemic necessitated the need for re-evaluation of the assets of the banks in uncertain conditions. The study did note that the said pandemic created uncertainty that required regulators to grant banks opportunities for implementing international standards on loan loss provisioning. However, this was a mere desk review study that focuses largely on review of related literature while relevant literature is reviewed in the present study to inform conceptualization of variables and design of the data

collection instruments which supported the analysis, conclusion and recommendations on credit risk management and liquidity.

Zheng, Perhiar, Gilal and Gilal (2019) placed focus on commercial banks in Pakistan and did an exploration of loan loss provisions and the risk-taking behavior of banks in the country. The specific focus of the study was on establishing key determinants of loan loss provision covering 22 banks in a period from 2010-2017. In this study, credit risk was measured as a proxy on sustainability and the risk-taking behavior of banks. The approach adopted in this study was quantitative and panel data was adopted. The study noted that inflation, lending interest rates and capital adequacy ratio were key determinants of loan loss provisioning. However, the focus of this study was on commercial banks in Pakistan while those in Kenya were explored as the context of the present study.

In a study that was done by Wil and Chau (2022) efficiency assessment was done through stochastic frontier analysis in 22 frontier market countries. After gathering and analysis of information through regression, it emerged that an inverse nexus exists between loan loss provisioning and efficiency. The implications drawn from these findings were that an expansion in loan loss provisioning strategies can enhance bank performance. However, the study covered efficiency as dependent variable and not liquidity thus the conceptual gap.

Magomere and Otinga (2019) analyzed the effect of loan loss provisioning capital adequacy, operating costs and their implication on financial performance with main focus on microfinance entities in Kakamega County in Kenya. More broadly, the determinants of financial performance of these institutions were explored using a survey design where 122 senior managers from 17 institutions were targeted. The analysis showed that loan loss provisioning, operating costs and capital adequacy were predictors of financial performance of the microfinance institutions. It was

recommended that efforts to enhance competitiveness of these institutions require them embrace viable loan loss provisioning practices like debt financing, providing for doubtful debts, loan loss reserves and adequate provisioning expenses. However, the study was done focusing on financial performance as the dependent variable that is conceptually different from liquidity which was used in the present study.

2.3.3 Lending Requirements and Liquidity

Sansa (2019) carried out an investigation in Tanzania with an analysis of loan conditions and access to loans by SMEs. The effect of bank loan extension procedures and access to loans was explored in this study leveraging qualitative as well as quantitative approaches. Respondents covered the customers of the banks and loan officers and their sampling was purposively done. Documentary reviews, interviews and questionnaires aided in data gathering. It was noted that bank established covenants that had an effect on ability of small firms to access loans. Besides, strict loan extension procedures affected access to loans by borrowers. This study however used interviews to support qualitative approach while the present study was purely quantitative in methodology.

Kiai et al. (2019) documented that collateral requirements negatively affected financial performance of small enterprises. However, the focus of the study was on financial performance as the dependent variable which is conceptually different from liquidity hence the gap. Zakayo and Ondabu (2022) indicated that lending had positive and significant effect on financial performance of listed banks in Kenya. The gap arising from this study however that is its focus was on listed banks which were only 12 in total while all the commercial banks in Kenya were covered in the proposed study.

Rithaa, Munene and Kariuki (2019) investigated the nexus between loan collateral requirements by banks and performance of small firms in Maua Town. While 250 enterprises were targeted, 153 were sampled and included in the analysis. Gathering of the information was supported by questionnaire. The analyzed and presented results were that loan collateral requirements had negative effect on financial performance of small firms.

2.3.4 Credit Risk Management, Political Risk and Liquidity

In Vietnam, Nguyen (2023) measured credit risk through non-performing loan ratio and loan loss provisioning ratio as well as capital adequacy ratio. After analysis and processing of the information that had been gathered, the study noted existence of inverse relationship between non-performing loan ratio and financial performance. However, loan loss provisioning and capital adequacy was not significant. The gap arising from this study is that it was done in Vietnam and not in Kenya.

Şanlısoy, Aydın, Yalçınkaya and Elif (2017) conducted an analysis into the implication of political risk on profitability of the bank in Turkey. Political risk index was used as a proxy of political risk. The analysis of the gathered results indicated existence of negative nexus between political risk and profitability of banks. The gap arising from this study is that its specific context was Turkey which is in the different continent compared to Kenya where the present study was conducted.

The study conducted in Nigeria by Obalade, Lawrence and Akande (2021) was an analysis of political risk and performance of banks. A total of 12 banks were selected within the period 2006-2018. The analysis of the gathered information was supported by a two-stage system of generalized method of moments. The study noted existence of inverse relationship between political risk and returns generated by the banks on their capitals. However, the link between

political risk and credit risk was found to be positive. However, performance and not liquidity was explored as the dependent variable and thus creating conceptual gap.

Mokaya, Jagongo, James and Ouma (2018) investigated the implication of political risk as a moderator in the nexus between bank attributes and lending rates in Kenya. The philosophy adopted in this study was positivism guided by an explanatory non-experimental research design. The targeted unit of analysis entailed 39 banks in Kenya where information in its secondary nature was obtained. The time period was 200 all through to 2015. The processing of the obtained information was supported by stata. After analysis, it was apparent that political risk had insignificant moderating effect in the link between bank attributes and lending rates.

2.3.5 Liquidity of Commercial Banks

Morina and Qarri (2021) identified the variables influencing Kosovo's commercial banks' liquidity. This study's primary goal is to examine the banking industry's sensitivity to various macroeconomic and banking variables in terms of liquidity. The study used regression analysis on a data set spanning eight years, from 2012 to 2019, in order to accomplish this goal. Following an analysis of the available data, the study noted that, of the primary factors influencing commercial banks' liquidity status, non-performing loans, capital adequacy, and credit interest rate had the biggest and most significant effects. However, this study covered commercial banks in Kosovo while the present study was on Kenya's commercial banks.

Karakas and Melek (2022) used data from the Turkish banking sector to assess how liquidity affected commercial banks' profitability. Twenty commercial banks that were active in Turkey between 2002 and 2020 were in total included in the study. According to the research, the ratio of liquid assets to current assets has a positive correlation with the return on assets ratio, while the

ratios of return on equity and net interest margin have a negative correlation. The ratio of acid-test assets to return on equity has a negative correlation with the return on assets ratio, while the ratio of loans to deposits has a negative correlation with all three profitability ratios. The study adopted profitability as the dependent variable which differ from liquidity adopted in the present study.

The impact of adequate liquidity on the financial performance of South Sudanese commercial banks was examined by Odongo and Irungu (2023). The study employed an explanatory research design. South Sudanese commercial banks were the target population. From 2017 to 2021, South Sudan had 29 commercial banks. Purposive sampling was employed in the study to select 23 banks that operated from 2017 to 2021. The results of the regression showed that operational adequacy was positively impacted by performance. According to the study, while certain returns are drawn to commercial banks by liquid assets, an excessive amount of them lowers banks' profitability levels. The context of this study was South Sudan while the present study was done in Kenya.

Abuga, Wamugo, and Makori (2023) examined the relationship between Kenyan commercial banks' financial performance and their liquidity capability. The explanatory research design was used in this investigation. The study's target population consisted of 42 Kenyan commercial banks. A data gathering procedure was used to obtain and compile the crucial financial data for analysis from the annual reports. Between 2012 and 2018, 42 commercial banks' panel data was mined during a six-year period. According to the results of the regression research, Kenyan commercial banks' financial performance is significantly improved by net stable funding and liquidity coverage.

2.4 Summary of Literature and Gaps

The chapter has reviewed a number of empirical studies from a global to regional and local point of view. However, these studies create knowledge gaps that were determined and presented as shown in Table 2.1.

Table 2.1: Summary of Literature and Gaps

Author	Study title	Key finding	Research gap	Focus of current study
Nguyen (2023)	measured credit risk through non-performing loan ratio and loan loss provisioning ratio as well as capital adequacy ratio	The study noted existence of inverse relationship between non-performing loan ratio and financial performance.	This study used financial performance as the dependent variable	Liquidity was the dependent variable in the present study
Odongo and Irungu (2023).	impact of adequate liquidity on the financial performance of South Sudanese commercial banks	while certain returns are drawn to commercial banks by liquid assets, an excessive amount of them lowers banks' profitability levels	The study was done in South Sudan	The present study was done in Kenya
Zakayo and Ondabu (2022)	Determined how lending affect financial performance of banks in Kenya	indicated that lending had positive and significant effect on financial performance of listed banks in Kenya	financial performance of banks in Kenya was the dependent variable	Liquidity was the dependent variable in the present study
Wil and Chau (2022)	Measured efficiency assessment through stochastic frontier analysis in 22 frontier market countries	it emerged that an inverse nexus exists between loan loss provisioning and efficiency.	This was cross country study	The present study was done in Kenya as a one country
Iakimenko, Semenova and Zimin (2022),	the link between information sharing and credit risk was explored.	The analysis indicated an existence of a nonlinear nexus between information disclosure and credit risk.	Credit risk was the dependent variable	Liquidity was the dependent variable in the present study
Karakas and Melek (2022)	used data from the Turkish banking sector to assess how liquidity affected commercial banks' profitability	the ratio of liquid assets to current assets has a positive correlation with the return on assets ratio, while the ratios of return on equity and net	The study was conducted in Turkey	The present study focused on Kenya as the context

De-Araujo, Cohen and Pogliani (2021)	focused on the COVID-19 pandemic and explored its implication on loan loss provisioning	interest margin have a negative correlation The study did note that the said pandemic created uncertainty that required regulators to grant banks opportunities for implementing international standards on loan loss provisioning.	Loan loss provisioning was adopted as the dependent variable	Liquidity was the dependent variable in the present study
Obalade, Lawrence and Akande (2021)	an analysis of political risk and performance of banks in Nigeria	noted existence of inverse relationship between political risk and returns generated by the banks on their capitals	This study was done in Nigeria that is more developed	The present study was done in Kenya
Morina and Qarri (2021)	identified the variables influencing Kosovo's commercial banks' liquidity.	of the primary factors influencing commercial banks' liquidity status, non-performing loans, capital adequacy, and credit interest rate had the biggest and most significant effects	This study was done in Kosovo	The present study was done in Kenya
Bonomo, Bruschi and Schechtman (2020)	carried a study on sharing of public and positive information and the implication on personal loans in Brazil.	It was noted after analysis that was done through ordinary least square that information asymmetry was a key factor shaping and influencing the interest rates charged by lenders	The study was done in Brazil	The present study was done in Kenya
Hung-Son, Gia –Khanh and Thanh-Liem (2020)	conducted a study on credit information sharing, corruption and financial development.	regression indicated that private credit bureaus and financial development are negatively related with each other	financial development was the dependent variable	Liquidity was the dependent variable in the present study
Magomere and Otinga (2019)	analyzed the effect of loan loss provisioning capital adequacy, operating costs and their implication on financial performance with main focus on microfinance entities in Kakamega County in Kenya.	The analysis showed that loan loss provisioning, operating costs and capital adequacy were predictors of financial performance of the microfinance institutions	The study covered microfinance institutions in Kakamega	Commercial banks in Kenya were central in the present study

Sansa (2019)	carried out an investigation in Tanzania with an analysis of loan conditions and access to loans by SMEs.	It was noted that bank established covenants that had an effect on ability of small firms to access loans	The study covered SMEs with their access to loans as the dependent variable	Liquidity was the dependent variable
Kiai et al. (2019)	Ascertained the effect of collaterals on financial performance	Documented that collateral requirements negatively affected financial performance of small enterprises.	Financial performance was the dependent variable	Liquidity was the dependent variable
Zheng, Perhiar, Gilal and Gilal (2019)	placed focus on commercial banks in Pakistan and did an exploration of loan loss provisions and the risk-taking behavior of banks in the country	The study noted that inflation, lending interest rates and capital adequacy ratio were key determinants of loan loss provisioning	The context of this study was Pakistan and the dependent variable was risk-taking behavior of banks	Kenya was the context of the present study with liquidity as the dependent variable
Rithaa, Munene and Kariuki (2019)	investigated the nexus between loan collateral requirements by banks and performance of small firms in Maua Town.	results were that loan collateral requirements had negative effect on financial performance of small firms.	Performance was the dependent variable	Liquidity was the dependent variable
Onsarigo (2018)	provided an indication that credit information sharing allowed lenders of funds to have access to reports linked with previous credit history and repayment patterns of borrowers.	the analyzed findings showed that SACCOs registered greater financial performance after the credit information bill was enacted than before when the same was passed.	The study was done among SACCOs	Commercial banks were covered in the present study
Mokaya, Jagongo, James and Ouma (2018)	conducted an investigation into the implication of political risk as a moderator in the nexus between bank attributes and lending rates in Kenya	it was apparent that political risk had insignificant moderating effect in the link between bank attributes and lending rates	Lending rates was the dependent variable	Liquidity was used as the dependent variable
Şanlısoy, Aydın, Yalçınkaya and Elif (2017)	conducted an analysis into the implication of political risk on profitability of the bank in Turkey.	results indicated existence of negative nexus between political risk and profitability of banks.	The study was done in Turkey	The present study was conducted in Kenya

Source: Empirical Literature Review (2024)

2.5 Conceptual Framework

Conceptual framework is a plan that guides and determines how variables of the study are conceptualized. Conceptual framework is Figure 2.1.

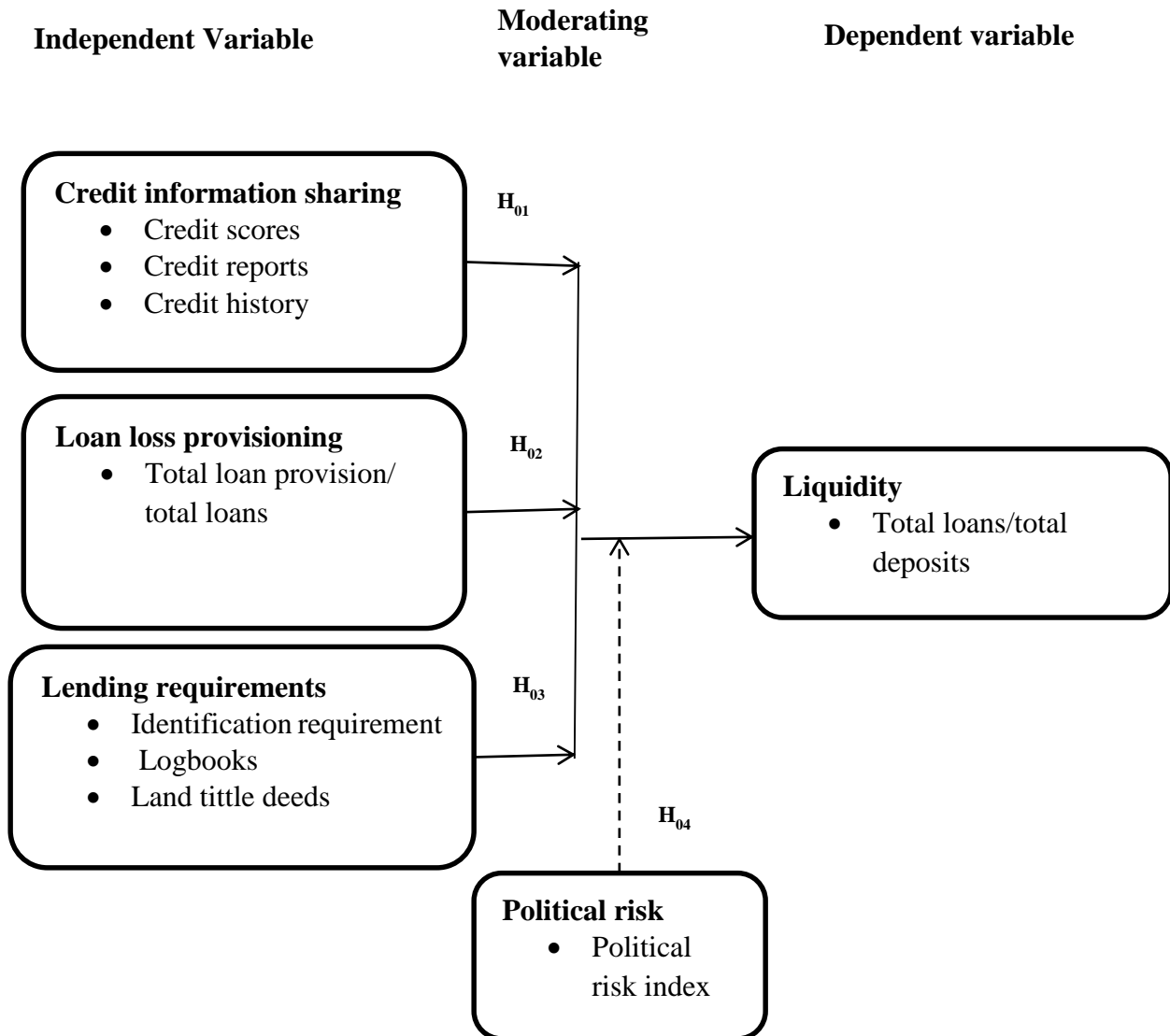


Figure 2.1: Conceptual Framework

Source: Researcher (2024)

From Figure 2.1, the three broad independent variables which were sub components of credit risk management that were covered included credit information sharing, loan loss provisioning and lending requirements. Credit information sharing was represented by credit scores, reports and

credit history. Loan loss provisioning was measured through total loan provision against total loans while identification requirement, logbooks and land title deeds were measures of lending requirements. Political risk a moderator variable was measured by the political risk index while liquidity was measured by total loans to total deposits.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The philosophy and design, empirical model and target population are detailed in this section. The other relevant contents covered in the chapter include targeted population, instrument of gathering information and the related procedures and data analysis and presentation. Ethical concerns are also detailed in the chapter.

3.2 Research Philosophy

Research philosophy defines overall notion and belief in regard to how statistics from a given issue need to be gathered, processed and used (Sardinha & Pinto, 2019). There are two broad categories and types of research philosophies: positivist and Interpretivism. In positivisms philosophy, reality is believed to be stable where one can easily observe and describe it from a point of view that is more objective without having interference on a phenomenon under investigation (McKinley & Rose, 2019). In this positivism philosophy, predictions are established based on previously explained and observed realities and their nexus (Thomas, Martin, Etnier & Silverman, 2022).

On the other, an interpretivism philosophy is where reality can only be comprehended through some kind of subjective interpretations (Nielsen, Eden & Verbeke, 2020). The analysis of a phenomena in its naturally occurring surrounding in critical in the interpretivism philosophy (Lo, Rey-Martí & Botella-Carrubi, 2020). Positivist research philosophy was adopted in this study. The reason for adopting this philosophy was because information for analysis was basically quantitative and there also be testing of hypotheses (Siedlecki, 2020). The key emphasis of the positivist philosophy is on studying and examining the causal interaction between the concerned

variables in a study. On this account, quantitative methods are much favoured by the positivists philosophy in a study (Siedlecki, 2020). Positivism philosophy guided and supported testing of hypotheses to draw relevant inferences on credit risk management and liquidity.

3.3 Research Design

Research design is defined as a structure that shape and inform the manner which data in the study is gathered and processed to yield evidence (Adams & McGuire, 2022). Explanatory research design was adopted in this study to attain formulated hypotheses. According to Dawson (2019), explanatory studies are concerned with providing an accurate description and account of the way things are in their original state without manipulation. Thus, the study leveraged this design to provide an accurate state of affairs on credit risk management and liquidity while supporting testing of the established hypotheses. This study entailed the use of multiple regression analysis, to predict the effect of credit risk on liquidity which could be best taken care through the explanatory design.

3.4 Empirical Model

Two regression models, direct effect model and moderated regression models guided the analysis of the findings in this study as discussed below:

3.4.1 Direct Effect Regression Model

Ordinary least square (OLS) direct effect regression model guided the analysis of the findings in the first step. According to Rose, McKinley and Baffoe-Djan (2019), an OLS regression is stable. Thus, OLS regression analysis was adopted to process the information that had been gathered in this study. The general and the product equations guided this analysis process as indicated in subsequent sections:

$$Y_{it} = \beta_0 + \beta_1 X_{1i} + \beta_2 X_{2it} + \beta_3 X_{3i} + \epsilon \quad (i)$$

Where:

Y_{it} = Liquidity of bank i at time t

β_0 = Constant term

$\beta_1 - \beta_3$ = Regression coefficients

X_{1i} = Credit information sharing of bank i

X_{2i} = Loan loss provisioning of bank i at time t

X_{3i} = Lending requirements of bank i

ϵ = error term

3.4.2 Moderating Effect Regression Model

The study had two-step regression model adapted from Baron and Kenny (1986). The models are specified as under: There were three key steps that were adhered to when testing for the moderating effect as listed below:

$$Y_{it} = \beta_0 + \beta_1 CRM_{1i} + \epsilon \quad (3.2)$$

Where:

Y_{it} = Liquidity of bank i at time t

β_0 = Constant term

$\beta_1 - \beta_3$ = Regression coefficients

CRM_{1i} = Credit Risk Management

ϵ = error term

$$Y_{it} = \beta_0 + \beta_1 CRM_{1i} + \beta_2 PR_{2it} + \epsilon \quad (3.3)$$

Where:

Y_{it} = Liquidity of bank i at time t

β_0 = Constant term

$\beta_1 - \beta_3$ = Regression coefficients

CRM_{it} = Credit Risk Management

PR_{it} = Political Risk

ϵ = error term

$$Y_{it} = \beta_0 + \beta_1 CRM_{it} + \beta_2 PR_{it} + \beta_3 CRM_{it} * PR_{it} + \epsilon \dots \dots \dots (3.4)$$

Where:

Y_{it} = Liquidity of bank i at time t

β_0 = Constant Term

$\beta_1 - \beta_3$ = Regression coefficients

CRM_i = Credit risk management (average mean values of credit information sharing, loan loss provisioning and lending requirements of bank i

PR_{it} = political risk of bank i at time t

$\beta_3 X_{it} * PR_i$ = interaction term of bank i and time t

ϵ = error term

The criteria for interpretation of the p-values during moderation testing is as given in Table 3.1:

Table 3.1: Moderation Testing Decision Making Criteria

Model	Inference
If p-value for $\beta_2 < 0.05$ in model 3.3	Partial moderation
If p-value for β_2 in model 2 and β_3 in model 3.4 are $p < 0.05$	Complete/full mediation

Source: Researcher (2024)

3.4.1 Operationalization and measurement of Variables

It is important to operationalize the variables of any study in order to inform the development of data collection tools. Table 3.2 gives a breakdown of operationalization.

Table 3.2: Operational Definition of Variables

Variable	Type	Brief Definition of term	Measurement	Measurement scale
Credit information sharing	Independent	a continuous process that occurs among existing financial institutions and the licensed credit referencing bureaus and it will be measured through credit scores, reports and credit history	<ul style="list-style-type: none"> • Credit scores • Credit reports • Credit history 	Ordinal
Loan loss provisioning	Independent	the amount of funds set aside to cushion the bank from non-performing loans and it will be measured in this study using the ratio of total loan provision against total loans	<ul style="list-style-type: none"> • loan provision/ total loans 	Ratio
Lending requirements	Independent	the conditions that borrowers must fulfil to qualify for a credit facility and they are represented in this study by identification requirement, logbooks and title deeds	<ul style="list-style-type: none"> • Identification requirement • Logbooks • Land title deeds 	Ordinal
Political risk	Moderating	the probability of loss of returns from investments as a result of unforeseen political events and it is measured in this study by the political risk index	<ul style="list-style-type: none"> • Given Political risk index from World Bank 	Ratio
Liquidity	Dependent	Loan deposit ratio	<ul style="list-style-type: none"> • $\text{Loan Deposit Ratio} = \frac{\text{Total Loans}}{\text{Total Deposits}}$ 	Ratio

Source: Researcher (2024)

3.5 Target Population

Collection of items that have similar attributes in common is generally called targeted population (Kara, 2020). The study targeted all the 39 commercial banks in Kenya operational as by end of December 2022 (CBK, 2023) as the unit of analysis while loan/credit managers or their equivalents from these institutions were unit of observation. This added up to 39 respondents.

3.6 Sampling Design

Sampling is the method that is conducted to select elements that need to be included in the study (Ghauri, Grønhaug & Strange, 2020). Since the target population can easily be accessed, census was undertaken as recommended by Thanem and Knights (2019).

3.7 Data Collection Instrument

Data collection instrument is a tool that helps in gathering the information required in the study for analysis (Privitera, 2022). The study gathered both primary and secondary and this ensured the flaw of one source of data is counteracted by another source. Questionnaire helped in gathering of primary data. Questionnaire collected information on credit information sharing and lending requirements. The descriptive nature of these variables justified the need for primary rather than secondary data. On the other hand, information on loan loss provisioning, political risk and liquidity was obtained from secondary sources guided by a data collection sheet on a period of 5-years being from 2018-2022. Secondary information on loan loss provisioning and liquidity was gathered from CBK and respective financial statements of the commercial banks while data on political risk was gathered from the reports available at the World Bank. The figure is usually computed on annual basis so it was simply picked across the respective years that this study covered.

3.8 Data Collection Procedure

An introduction letter from Kenyatta University was sought in advance before commencing the data gathering exercise from respondents. This in turn was followed by a permit of conducting the research from NACOSTI that was used to state the purpose of the study as for academic reason. Questionnaire was administered to respondents by self, a strategy aimed at increasing the response rate. On the other hand, secondary data on political risk index and liquidity was gathered from World Bank publications.

3.9 Validity and Reliability of the Research Instrument

An instrument of research is said to have validity when it measures an aspect which it is designed to indicate (Kara, 2020). The questionnaire was shared with supervisor and experts in the field of finance who reviewed contents to ensure they were adequate and in line with the theories and the literature reviewed. The study instrument is deemed as reliable when it provides measurement that is consistent even when the same has been done after successive trials (Eden & Nielsen, 2020). In this study, a pilot study was conducted among 4 credit managers from commercial banks in Kenya being 10% of the study sample as recommended by Dźwigoł (2019). These respondents in the pilot study were excluded in the final study as a way of limiting biasness and their selection was purposively. The results from this pilot study helped in computation of the values of Cronbach Alpha coefficients and such figures above 0.7 signified reliability of the study tool as suggested by Strijker, Bosworth and Bouter (2020).

3.10 Data Analysis and Presentation

The information gathered both from respondents and from existing secondary sources was keyed into SPSS in readiness for analysis that was achieved through descriptive and regression. Rationale of use of regression was because it was the most ideal method of testing hypotheses in a study so as to draw informed inferences regarding the significance of the variables under consideration. The key descriptive statistics that were adopted include means and standard deviations while multiple regression analysis formed the inferential statistic. Tables helped to present the findings of the study.

3.10.1 Diagnostic Tests

For Multicollinearity, VIF values were computed and interpreted accordingly in testing this assumption. According to Harris, Holyfield, Jones, Ellis and Neal (2019), such VIF values in the

range of 1-10 imply absence of this assumption in the sample data otherwise such values above 10 would justify existence of the symptom. Normality was determined through Shapiro-Wilk test and when $p > 0.05$, the null hypothesis is rejected and the presence of normality is assumed (Bougie & Sekaran, 2019). Heteroscedasticity test was conducted to establish presence or absence or constancy or variation in error term and its absence is undesirable in the data. Levene test was conducted to validate this assumption where $p > 0.05$ signified absence of this condition (Liamputtong, 2019) and thus the presence of Homoscedasticity was assumed. Otherwise, the null hypothesis was presence of Heteroscedasticity.

3.11 Ethical Considerations

In conducting this study, a number of ethical issues needed to be adhered to. To begin with, information reviewed was cited appropriately with aim of avoiding plagiarism. Participation in the study was on a free and voluntary basis and hence no one was forced to do so. Information obtained from respondents was confidential. No participant was obliged to disclose name on the questionnaire so as to safeguard their privacy and confidentiality.

CHAPTER FOUR

DATA ANALYSIS AND DISCUSSION

4.1 Introduction

This chapter is set out to provide the analysis of findings based on the specific objectives that were set out. It covers the response rate, analysis of descriptive statistics, diagnostic tests, correlation and regression results. It also captures discussion of the findings that is done by interacting with the reviewed literature. The study collected both primary and secondary data, guided by ordinal and ratio scales respectively. During multiple regression analysis, average values of secondary data per variables across the 5-year period were computed while the ordinal scale for primary data was transformed into continuous scales. Since primary data had been collected per commercial banks, this made it easier to integrate with the average values from secondary data that had been computed and thus making it easier to perform the multiple regression analysis. Complete response from primary data was obtained from 35 commercial banks, and their relevant average secondary data across the 5-year period were used to support regression analysis.

4.2 Reliability Results

Table 4.1 gives an overview of the reliability results:

Table 4.1: Reliability Results

Variable	No of items	Cronbach Alpha Coefficient
Credit information sharing	4	.765
Lending requirements	4	.779

Source: Research Data (2024)

Table 4.1 indicates that all the variables of the study had values of Cronbach Alpha coefficients above 0.7. This concurs with Strijker, Bosworth and Bouter (2020) who noted that an above 0.7 value of Cronbach Alpha indicate that the scale adopted in the study is a reliable one.

4.3 Response Rate

Table 4.2 is an overview of the response rate.

Table 4.2: Response Rate

Response Rate	Frequency	Percentage
Response	35	89.7%
Non-response	4	10.3%
Total	39	100.0

Source: Research Data (2024)

The study targeted 39 respondents from commercial banks in Kenya and 35 of them were completely filled in and returned. This was equivalent to a response rate of 89.7% which was adequate and consistent with Babbie (2010) who noted that an above 80% response rate is excellent to support the analysis and presentation of findings in a study.

4.4 Analysis of General Information

The general information of the respondents who took part in the study were determined and presented as shown in Table 4.3. These covered the distribution of respondents by their gender, levels of education and years of experience.

Table 4.3: General Information

General Information	Frequency	Percentage
Male	20	57.1%
Female	15	42.9%
Level of education		
Certificate	9	25.7%
Diploma	11	31.4%
Degree	13	37.1%
Masters and above	7	20.0%
Years of experience		
Less than 5 years	5	14.3%
6-10 years	7	20.0%
10-15 years	11	31.4%
Over 15 years	12	34.3%

Source: Research Data (2024)

The findings in Table 4.3 indicate that 57.1% of the respondents were male and 42.9% were female. This means that there was gender diversity which is one of the requirements of the Constitution of Kenya (2010) on gender inclusion. It was established that 37.1% had degrees, 31.4% had diplomas, 25.7% had certificates and 20% had masters and above. This means that respondents who took part in the study. On the other hand, while 34.3% had worked for over 15 years, 31.4% had worked for 10-15 years, 2-% for 6-10 years and 14.3% for less than 5 years. These findings mean that there was gender diversity in the study with respondents having different gender categories coupled with their education and level of experience they had accumulated in the banking sector at large.

4.5 Descriptive Statistics

The findings of descriptive statistics determined through means and standard deviations were established and summarized as shown in the subsequent sections.

4.5.1 Credit Information Sharing

The findings in Table 4.3 indicate descriptive statistics on credit information sharing which was the first independent objective variable that guided the study.

Table 4.4: Credit Information Sharing

Statements on Credit Information Sharing	Min	Max	Mean	Std. Dev
Credit scores of customers	2.00	5.00	3.71	.750
Internal credit reports	1.00	5.00	3.69	1.116
Credit history of customers	2.00	5.00	3.68	.847
Credit reports from Credit Reference Bureaus (CRBs)	2.00	5.00	3.65	.764

Source: Research Data (2024)

Table 4.4 indicates that respondents agreed that credit scores (M=3.71), credit reports (M=3.69), credit history (M=3.68) as well as credit reports from Credit Reference Bureaus (CRBs) (M=3.65) were all established as critical components of credit information sharing. This implies that credit

scores, credit history and CRBs were important elements of credit information sharing that had been adopted by commercial banks. These findings agree with Bowen and Makokha (2021) who noted that credit information sharing provide mechanisms where lenders have an opportunity of assessing borrowers' reports from the Credit Reference Bureaus that provides more information on repayment patterns of customers. In Kenya for instance, some of the CRBs include Metropol as well as TranzUnion among others and they provide such services as the credit scores, credit reports and credit histories as well as the clearance certificates for the defaulted clients.

4.5.2 Lending Requirements

The findings of descriptive statistics on lending requirements were determined and presented as shown in Table 4.5

Table 4.5: Lending Requirements

Statements on Lending Requirements	Min	Max	Mean	Std. Dev
National identification cards of the loan applicants	2.00	5.00	3.88	.932
Passport photographs	2.00	5.00	3.60	.881
Logbooks	3.00	5.00	3.94	.5915
Land title deeds	2.00	4.00	3.65	.683

Source: Research Data (2024)

The findings in Table 4.5 indicate that logbooks (M=3.94), national identification card (M=3.88) as well as land title deed (M=3.65) and passport photos (M=3.60) were important lending requirements in the studied institutions. These findings imply that financial institutions in deed relied on a number of items as collaterals before advancing credit facilities to loan applicants. The finding agree with Fraisse, Lé and Thesmar (2020) who noted that lending requirements include the national identity cards, official pay-slips and log books or land title deeds among others. Other common lending requirements according to Golubeva, Duljic and Keminen (2019) that commercial banks require from borrowers during the loan appraisal process include their

identification requirements like the passports, their levels of income and the amount of their collaterals.

4.5.3 Loan Loss Provisioning, Political Risk and Liquidity

Descriptive statistics on secondary data that was gathered in this study were computed and summarized as indicated in Table 4.6.

Table 4.6: Loan Loss Provisioning, Political Risk and Liquidity

Statements on Loan Loss Provisioning, Political Risk and Liquidity	Min	Max	Mean	Std. Dev
Loan Loss Provision	.00	.53	.1767	.13556
Political Risk Index	.10	.38	.1804	.05473
Liquidity	.00	.04	.0078	.00897

Source: Research Data (2024)

The findings in Table 4.6 indicate values as follow: loan loss provision (M=0.1767), political risk index (M=0.1804) and (M=0.0078) respectively. This means that the was loan loss provisioning had been set aside by the studied financial institutions. This loan loss provisioning is setting of an expense in the income statement of the financial institution that cushions the uncollected loans and payments Danisman, Demir & Ozili, 2021). In order to present an accurate picture of the financial status, commercial banks are mandated to provide an account of all expenses and loan defaults hence the need for loan loss provisioning in the financial statements (Nugroho, Arif & Halik, 2021).

4.6 Diagnostic Tests

The study performed multicollinearity, normality and Heteroscedasticity test with the findings as presented in subsequent sections:

4.6.1 Multicollinearity Test

For Multicollinearity, VIF values were computed and interpreted accordingly in testing this assumption. According to Harris, Holyfield, Jones, Ellis and Neal (2019), such VIF values in the range of 1-10 imply absence of this assumption in the sample data otherwise such values above 10 justified existence of the symptom. The finding in Table 4.7 gives an overview of the outcome after computation.

Table 4.7: Multicollinearity Test

Multicollinearity Test	Collinearity Statistics	
	Tolerance	VIF
Credit Information Sharing	.863	1.159
Lending Requirements	.556	1.799
Loan Loss Provision	.787	1.270
Political Risk Index	.680	1.470

Source: Research Data (2024)

In testing multicollinearity, H_0 : there is no multicollinearity and H_1 : there is multicollinearity. From Table 4.7, the VIF values for credit information sharing, lending requirements, loan loss provisioning and political risk index were 1.159, 1.799, 1.270 and 1.470 respectively. As each of these values are all in the range of 1-10, it can be asserted that there was no multicollinearity weakness in the sample data that was used in this study. Thus hypothesis H_0 was accepted.

4.6.2 Normality Test

Normality was determined through Shapiro-Wilk test and when $p > 0.05$, the null hypothesis is rejected and the presence of normality is assumed (Bougie & Sekaran, 2019). The findings of analysis were determined and summarized as shown in Table 4.8.

Table 4.8: Normality Test

Normality Test	Skewness		Kurtosis	
	Statistic	Std. Error	Statistic	Std. Error
Credit Information Sharing	1.463	.398	1.567	.778
Loan Loss Provision	1.811	.398	1.872	.778
Lending Requirements	.222	.398	-1.157	.778
Political Risk Index	.635	.398	-.139	.778
Credit Risk Management	.210	.398	-1.143	.778
Interaction Term	1.495	.398	1.290	.778
Liquidity	1.783	.398	1.844	.778

Source: Research Data (2024)

H₀: there is no normality; H₁: there is normality

The findings in Table 4.8 indicate that all the values of Skewness and Kurtosis were in the range of +/-3, this means that there was normality as an assumption guiding regression analysis in the data that as adopted in this study. Therefore, hypothesis H₀ was rejected and an inference of presence of normality was drawn.

4.6.3 Heteroscedasticity test

Heteroscedasticity test is conducted to establish presence or absence or constancy or variation in error term and its absence is undesirable in the data. Levene test was conducted to validate this assumption where $p > 0.05$ signified absence of this condition (Liamputtong, 2019) and thus the presence of Homoscedasticity was assumed. Otherwise, the null hypothesis was presence of Heteroscedasticity. Table 4.6 is an overview of the results that were obtained after analysis. This was determined through Figure 4.1 which is scatter plot and Figure 4.1 which is the outcome from Levene test respectively.

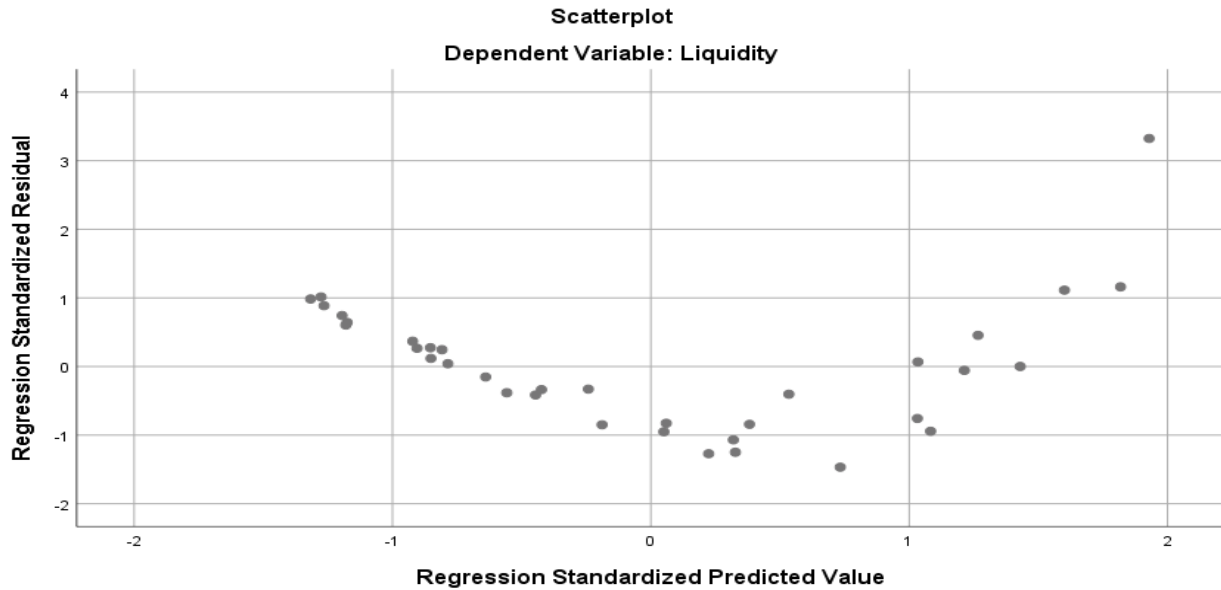


Figure 4.1: Scatter Plot

Source: Research Data (2024)

H_0 : there is no Heteroscedasticity, H_1 : there is Heteroscedasticity,

The findings from Figure 4.1 above indicate that there is clearly established and known pattern from the spread of data points. This indicates that there was absence of Heteroscedasticity in the data that was used to carry out regression analysis in this study. Thus, hypothesis H_0 was rejected.

4.7 Correlation Analysis

The strength and direction of relationship between credit risk management and liquidity of commercial banks in Kenya were determined through correlation analysis with findings as presented in Table 4.9.

Table 4.9: Correlation Analysis

		Liquidity	Credit information sharing	Loan loss provisioning	Lending requirements	Political risk
Liquidity	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	35				
Credit information sharing	Pearson Correlation	.567	1			
	Sig. (2-tailed)	.000				
	N	35	35			
Loan loss provisioning	Pearson Correlation	.760	.359*	1		
	Sig. (2-tailed)	.000	.034			
	N	35	35	35		
Lending requirements	Pearson Correlation	.746	.348*	.136	1	
	Sig. (2-tailed)	.000	.040	.435		
	N	35	35	35	35	
Political risk	Pearson Correlation	.506	.140	.076	.142	1
	Sig. (2-tailed)	.000	.424	.663	.415	
	N	35	35	35	35	35

Table 4.9 indicate that credit information sharing had strong and positive correlation with liquidity of commercial banks $r=0.567$. Loan loss provisioning $r= 0.760$ also had strong and positive relationship with liquidity. Similarly, lending requirement $r=0.746$ as well as political risk $r=0.606$ all had strong and positive correlation with liquidity. It then follows that credit risk management is a strong and positive correlate of liquidity of commercial banks in Kenya.

4.8 Regression Results

The subsequent sections detail the findings of regression analysis testing the direct and moderating effect between the study variables:

4.8.1 Direct Effect of Credit Risk Management and Liquidity

Regression analysis was performed to aid in testing of the formulated objectives. The outputs from this covered model summary, Analysis of Variance and regression beta coefficients and significance. The findings from model summary results are as presented in Table 4.10.

Table 4.10: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.886a	.786	.757	.00609

Source: Research Data (2024)

From Table 4.10, the value of adjusted R-square 0.757, this means that 75.7% change in liquidity management among commercial banks can be explained by their credit risk management. This means that there are other additional factors aside from credit risk management that have an effect on liquidity of these institutions and the focus of future studies should be on establishing these factors. The findings of ANOVA were determined and presented as shown in Table 4.11.

Table 4.11: ANOVA Findings

ANOVA	Sum of Squares	df	Mean Square	F	Sig.
Regression	.004	4	.001	27.523	.000 ^b
Residual	.001	30	.000		
Total	.005	34			

Source: Research Data (2024)

From Table 4.11, the p-value is 0.000 which is less than 0.05; this means that on overall, the regression model that was adopted in this study was significant. Table 4.12 is a breakdown of the results of beta coefficients and significance:

Table 4.12: Beta Coefficients and Significance

Variables	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	-.294	.083		-3.542	.000
Credit Information	.110	.018	.111		.032
Sharing				6.111	
Loan Loss	.127	.021	.119		.020
Provision				6.048	
Lending	.121	.012	.964		.000
Requirements				2.327	

Source: Research Data (2024)

From Table 4.12, the following regression model is predicted and fitted between credit risk management and liquidity of commercial banks in Kenya:

$$Y_{it} = -0.294 + 0.110X_{1i} + 0.127X_{2it} + 0.121X_{3i} + \epsilon \quad (i)$$

Where:

Y_{it} = Liquidity of bank i at time t

β_0 = Constant term

$\beta_1 - \beta_3$ = Regression coefficients

X_{1i} = Credit information sharing of bank i

X_{2i} = Loan loss provisioning of bank i at time t

X_{3i} = Lending requirements of bank i

ϵ = error term

From the findings in Table 4.10, the study noted that a decrease in credit risk management when other factors are held constant would lead to an improvement when all factors are held constant, a unit increase in credit information sharing other factors held constant can enhance liquidity of commercial banks in Kenya by 0.110 units. It also emerged that a unit increase in loan loss provisioning other factors kept constant can enhance liquidity by 0.127 units. It also emerged that a unit increase in lending requirements with other factors kept constant can enhance liquidity of commercial banks by 0.121 units.

4.8.2 Product Model Testing for Moderation of Political Risk

In this study, the moderating effect of political risk was determined through product regression model with findings as presented in Table 4.13.

Table 4.13: Product moderated Model

Models	R			Std. Error of the Estimate	Change Statistics				
	R	Adjusted R Square	Adjusted R Square		R Square Change	F Change	df1	df2	Sig. F Change
1	.378 ^a	.143	.117	1.07753	.143	5.487	1	33	.025
2	.791 ^b	.626	.603	.72259	.484	41.381	1	32	.000
3	.832 ^c	.691	.662	.66689	.065	6.568	1	31	.015

a. Predictors: (Constant), Loan Loss Provision

b. Predictors: (Constant), Loan Loss Provision, Political Risk Index

c. Predictors: (Constant), Loan Loss Provision, Political Risk Index, Interaction Term

Source: Research Data (2024)

From Table 4.13, there was an R square change of 0.143 in model 1, 0.484 in model 2 and 0.065 in model 3. This R square change is an implication of possibility of political risk as a moderator variable that was adopted in this study. The ANOVA findings in this study were determined and summarized as shown in Table 4.14.

Table 4.14: ANOVA Findings

		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6.371	1	6.371	5.487	.025 ^b
	Residual	38.315	33	1.161		
	Total	44.686	34			
2	Regression	27.977	2	13.989	26.791	.000 ^c
	Residual	16.709	32	.522		
	Total	44.686	34			
3	Regression	30.899	3	10.300	23.158	.000 ^d
	Residual	13.787	31	.445		
	Total	44.686	34			

a. Dependent Variable: Liquidity

b. Predictors: (Constant), Loan Loss Provision

c. Predictors: (Constant), Loan Loss Provision, Political Risk Index

d. Predictors: (Constant), Loan Loss Provision, Political Risk Index, Interaction Term

Source: Research Data (2024)

The findings in Table 4.14 indicate the values of F-calculated as 5.487, 26.791 as well as 23.158 which are all above F critical values. This is an implication that the overall regression models in this study were all significant. The value of ANOVA was determined and findings presented as shown in Table 4.15.

Table 4. 15: ANOVA Findings

Model		Unstandardized Coefficients		Standardized Coefficients		t	Sig.
		B	Std. Error	Beta			
1	(Constant)	27.169	.636			42.744	.000
	Credit Risk Management	-7.909	3.377	-.378		-2.342	.025
	(Constant)	14.648	1.993			7.351	.000
2	Credit Risk Management	-2.782	2.401	-.133		-1.159	.255
	Political Risk Index	.167	.026	.737		6.433	.000
	(Constant)	-327.191	133.392			-2.453	.020
3	Credit Risk Management	-2.180	2.228	-.104		-.978	.335
	Political Risk Index	.102	.035	.450		2.926	.006
	Interaction Term	.206	.081	.392		2.563	.015
	(Constant)						

a. Dependent Variable: Liquidity

Source: Research Data (2024)

The findings in Table 4.15 indicate that in model 1, credit risk management is found to be significant ($p < 0.05$). In model 2, political risk ($p < 0.05$) was also found to be significant. In model 2, political risk and interaction term were all found to be significant ($p < 0.05$). It then follows that political risk is a significant moderating variable in the relationship between credit risk management and liquidity.

4.9 Hypotheses Testing

A discussion of the findings based on the hypothesis is as set out below:

4.9.1 Credit Information Sharing and Liquidity

The first hypothesis of the study was H_{01} : credit information sharing has no significant effect on liquidity of commercial banks in Kenya. From the findings, credit information sharing had p-value given as 0.032, that is $p < 0.05$ and hence it was significant. Thus, it can be inferred that credit information sharing was a significant predictor of liquidity of commercial banks in Kenya. These findings contradict with Hung-Son, Gia –Khanh and Thanh-Liem (2020) who noted that public

credit registries were insignificantly linked with financial development. Iakimenko, Semenova and Zimin (2022) indicated that an increase in depth of credit information disclosure decreases credit risk. Bonomo, Bruschi and Schechtman (2020) noted after analysis that was done through ordinary least square that information asymmetry was a key factor shaping and influencing the interest rates charged by lenders. Onsarigo (2018) showed that SACCOs registered greater financial performance after the credit information bill was enacted than before when the same was passed.

4.9.2 Loan Loss Provisioning and Liquidity

In the second hypothesis, the focus was that H₀₂: loan loss provisioning has no significant effect on liquidity of commercial banks in Kenya. The findings indicated the p-value as p=0.020 which is less than 0.05. Thus, this study deduced that loan loss provisioning had significant effect on liquidity of commercial banks in Kenya. The finding is in line with Zheng, Perhiar, Gilal and Gilal (2019) who noted that inflation, lending interest rates and capital adequacy ratio were key determinants of loan loss provisioning. Wil and Chau (2022) indicated that an expansion in loan loss provisioning strategies can enhance bank performance. Magomere and Otinga (2019) showed that loan loss provisioning, operating costs and capital adequacy were predictors of financial performance of the microfinance institutions.

4.9.3 Lending Requirements and Liquidity

The third hypothesis of the study was H₀₃: lending requirements have no significant effect on liquidity of commercial banks in Kenya. The results in Table 4.10 indicated the p-value under this objective as p=0.000 i.e. p<0,05. Thus, the study rejected hypothesis H₀₃ deducing that lending requirements in deed had significant effect on liquidity. The finding is consistent with Sansa (2019) who was of the view that the bank established covenants that had an effect on ability of

small firms to access loans. Kiai et al. (2019) documented that collateral requirements negatively affected financial performance of small enterprises. Zakayo and Ondabu (2022) indicated that lending had positive and significant effect on financial performance of listed banks in Kenya. Rithaa, Munene and Kariuki (2019) indicated that loan collateral requirements had negative effect on financial performance of small firms.

4.9.4 Credit Risk Management, Political Risk and Liquidity

The fourth hypothesis of the study was H₀₄: political risk has no significant moderating effect on relationship between credit risk management and liquidity of commercial banks in Kenya as p-values in the three models above were all less than 0.05. The finding is consistent with Nguyen (2023) who noted existence of inverse relationship between non-performing loan ratio and financial performance. The study conducted in Nigeria by Obalade, Lawrence and Akande (2021) noted existence of inverse relationship between political risk and returns generated by the banks on their capitals. Mokaya, Jagongo, James and Ouma (2018) noted that political risk had insignificant moderating effect in the link between bank attributes and lending.

4.10 Discussion of Key Findings

. From the findings, credit information sharing had p-value given as 0.032, that is $p < 0.05$ and hence it was significant. Thus, it can be inferred that credit information sharing was a significant predictor of liquidity of commercial banks in Kenya. These findings contradict with Hung-Son, Gia –Khanh and Thanh-Liem (2020) who noted that public credit registries were insignificantly linked with financial development. Iakimenko, Semenova and Zimin (2022) indicated that an increase in depth of credit information disclosure decreases credit risk. Bonomo, Bruschi and Schechtman (2020) noted after analysis that was done through ordinary least square that information asymmetry was a key factor shaping and influencing the interest rates charged by lenders. Onsarigo (2018) showed

that SACCOs registered greater financial performance after the credit information bill was enacted than before when the same was passed.

The findings indicated the p-value as $p=0.020$ which is less than 0.05. Thus, this study deduced that loan loss provisioning had significant effect on liquidity of commercial banks in Kenya. The finding is in line with Zheng, Perhiar, Gilal and Gilal (2019) who noted that inflation, lending interest rates and capital adequacy ratio were key determinants of loan loss provisioning. Wil and Chau (2022) indicated that an expansion in loan loss provisioning strategies can enhance bank performance. Magomere and Otinga (2019) showed that loan loss provisioning, operating costs and capital adequacy were predictors of financial performance of the microfinance institutions.

The results indicated the p-value under this objective as $p=0.000$ i.e. $p<0,05$. Thus, the study rejected hypothesis H_03 deducing that lending requirements in deed had significant effect on liquidity. The finding is consistent with Sansa (2019) who was of the view that the bank established covenants that had an effect on ability of small firms to access loans. Kiai et al. (2019) documented that collateral requirements negatively affected financial performance of small enterprises. Zakayo and Ondabu (2022) indicated that lending had positive and significant effect on financial performance of listed banks in Kenya. Rithaa, Munene and Kariuki (2019) indicated that loan collateral requirements had negative effect on financial performance of small firms.

The p-values in the three models above were all less than 0.05 thus political risk was significant moderator. The finding is consistent with Nguyen (2023) who noted existence of inverse relationship between non-performing loan ratio and financial performance. The study conducted in Nigeria by Obalade, Lawrence and Akande (2021) noted existence of inverse relationship between political risk and returns generated by the banks on their capitals. Mokaya, Jagongo,

James and Ouma (2018) noted that political risk had insignificant moderating effect in the link between bank attributes and lending.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The chapter covers the summary and conclusion of findings. Recommendations and areas that required further research are also pointed out in this chapter as set out below. Limitations of mixed approach included difficulties in merging and integration of both primary and secondary data with different scales. To address this concern, relevant responses from primary data per bank were used to guide collection of secondary data which was averaged to align with first hand data.

5.2 Summary

5.2.1 Credit Information Sharing and Liquidity

The findings of descriptive statistics indicate that respondents agreed that credit scores, credit reports, credit history as well as credit reports from Credit Reference Bureaus (CRBs) were all established as critical components of credit information sharing. This implies that credit scores, credit history and CRBs were important elements of credit information sharing that had been adopted by commercial banks. In Kenya for instance, some of the CRBs include Metropol as well as TranzUnion among others and they provide such services as the credit scores, credit reports and credit histories as well as the clearance certificates for the defaulted clients. From the findings, credit information sharing was a significant predictor of liquidity of commercial banks in Kenya.

5.2.2 Loan Loss Provisioning and Liquidity

The findings indicate values as follow: loan loss provision was at an efficient level. , This loan loss provisioning is setting of an expense in the income statement of the financial institution that cushions the uncollected loans and payments. The findings indicated the loan loss provisioning had significant effect on liquidity of commercial banks in Kenya.

5.2.3 Lending Requirements and Liquidity

The findings indicate that logbooks, national identification card as well as land title deed and passport photos were important lending requirements in the studied institutions. These findings imply that financial institutions in deed relied on a number of items as collaterals before advancing credit facilities to loan applicants. The results were that lending requirements in deed had significant effect on liquidity.

5.2.4 Credit Risk Management, Political Risk and Liquidity

Political risk was relatively not so high, except for the recent incidences of the anti-Finance Bill of 2024 protests that left hundreds of people injured with death in some incidence. Political risk is not good for economic growth as it can result into capital flight. High level of political risk can increase the cost of living in the country. It emerged from regression analysis that political risk is a significant moderator variable in the relationship between credit risk management and liquidity.

5.3 Conclusion

Conclusion of the findings as informed by the specific objectives of the study is provided below per objective:

5.3.1 Credit Information Sharing and Liquidity

Credit information sharing had positive beta coefficient, implying that an improvement in credit sharing mechanisms of commercial banks in Kenya can allow them to be more liquid. Being significant, it implies that any efforts to enhance credit information sharing would also result into greater liquidity. This conclusion concurs with the information asymmetry theory, that advances the need for credit information sharing to counter moral hazard and adverse selection problem especially in commercial banks that are actively involved in lending operations.

5.3.2 Loan Loss Provisioning and Liquidity

Loan loss provisioning was found to have a positive beta coefficient; this means that any increase in this parameter would also lead to an enhancement in the level of liquidity. In particular, the study noted that increasing loan loss provisioning is the most way of supporting the liquidity requirements of the commercial banks in Kenya. This conclusion advances the transaction cost theoretical lens which imply that loan loss provisioning could be part of transaction costs incurred by financial institutions in their financial intermediation role in an economy like Kenya.

5.3.3 Lending Requirements and Liquidity

Lending requirements had positive beta coefficient, implying that investing resources to improve the same can result into an improvement in the liquidity level. Being significant, it implies that strengthening and increasing the loan loss provisions can also contribute towards a highly liquid position of the banks in question. This conclusion aligns with the transaction cost theory that implicitly mean commercial banks pass some of the transaction costs to customers in terms of struct lending requirements in order to facilitate financial intermediation in an economy.

5.3.4 Credit Risk Management, Political Risk and Liquidity

The study concludes that credit risk management is an important practice that has potential to positively influence liquidity. It was concluded that having in place a strong credit risk management framework can greatly enhance liquidity levels of institutions which in turn can enhance stability and soundness of a financial institution. Thus, in order to continue shaping and influencing the soundness of a financial institution like a commercial bank, it is of greater importance to attach more emphasis on improving credit risk management mechanisms that are in place. Consistent with the modern portfolio theoretical lens, it can be concluded that an effective

risk management framework in lending institutions like commercial banks contribute towards maximization of returns.

5.4 Policy Recommendations

Based on the findings, the study suggests the following recommendations:

5.4.1 Credit information Sharing and Liquidity

The Credit Managers working among commercial banks in Kenya should invest in latest technologies for carrying out timely credit information of customers with the licensed Reference Bureaus. This is expected to have significant effect on the level of liquidity which in turn would contribute to overall stability. These managers should tap into the power of credit scores, reports and histories of customers to provide reliable credit services which in turn would lead to uptake of loan facilities and thus financial stability.

5.4.2 Loan Loss Provisioning and Liquidity

The study noted existence of significant nexus between loan loss provisioning and liquidity. In regard to this finding, it is recommended that loan officers working with commercial banks in Kenya should diversify into loan portfolio in order to remain stable and have meaningful contribution to the growth of an economy.

5.4.3 Lending Requirements and Liquidity

The study identified lending requirements as playing an instrumental role towards the liquidity. Hence, this study recommends that managers working with commercial banks in Kenya should effectively invest in lending requirements like land title deeds and logbooks in order to improve on their credit risk management which in turn can allow them achieve optimal and required liquidity levels.

5.4.4 Credit Risk Management, Political Risk and Liquidity

The study identified political risk to be a significant moderator variable. Thus, it is recommended that the government of Kenya should seek to improve on the existing political environment in the country so as to positively influence liquidity level and thus promoting financial stability of the commercial banks.

5.5 Contribution to Knowledge

The present study has contributed to the body of knowledge in two ways. First, it is clear that cultivating an environment that enhance credit risk management of commercial banks can in turn enhance the level of liquidity of the commercial banks. In particular, it was evident that any investment in credit information sharing and loan loss provisioning as well as lending requirements would in turn improve liquidity position and levels of commercial banks in Kenya. Secondly, the positive spillover effects from credit risk management can be moderated by political risk. This time when the political atmosphere in a country is fragile, defaulting can increase thus worsening the said effects of credit risk management among commercial banks in Kenya.

5.6 Areas for Further Research

The present study covered all commercial banks in Kenya. Thus, there is need for further studies to be done covering other financial institutions like microfinance banks, Savings and Credit Cooperatives among others in order to improve on representativeness and applicability of the findings. Apart from covering the banking and financial sector, future studies should be conducted on other institutions like manufacturing firms or the non-financial firms. This will provide the basis for generalization of findings.

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APPENDICES

Appendix I: Research Authorization Letter



**KENYATTA UNIVERSITY
OFFICE OF THE EXECUTIVE DEAN GRADUATE SCHOOL**

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

Website: www.ku.ac.ke

P.O. Box 43844, 00100
NAIROBI, KENYA
Tel. 020-8704150

Our Ref: D58F/CTY/PT/21645/2022

DATE: 20th August 2024

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

Dear Sir/Madam,

**RE: RESEARCH AUTHORIZATION FOR MR. WARSAME MOHAMMED
OSMAN REG. NO. D58F/CTY/PT/21645/2022**

I write to introduce Mr. Warsame Mohammed Osman who is a Postgraduate Student of this University. He is registered for M.sc degree programme in the Department of Accounting and Finance.

Mr. Warsame Mohammed Osman intends to conduct research for a M.sc. Thesis Proposal entitled, *"Credit Risk Management and Liquidity of Commercial Banks in Kenya"*.

Any assistance given will be highly appreciated.

Yours faithfully,


for **PROF. ELJUD N.M. NJAGI**
AG. EXECUTIVE DEAN, GRADUATE SCHOOL

Appendix II: Approval Letter from KU



KENYATTA UNIVERSITY
OFFICE OF THE EXECUTIVE DEAN GRADUATE SCHOOL

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

P.O. Box 43844, 00100

Website: www.ku.ac.ke

NAIROBI, KENYA
Tel. 020-8704150

Internal Memo

FROM: Executive Dean, Graduate School DATE: 20th August 2024
TO: Mr. Warsame Mohammed Osman REF: D58F/CTY/PT/21645/2022
c/o Department of Accounting and Finance

SUBJECT: APPROVAL OF RESEARCH PROPOSAL

=====

This is to inform you that Graduate School Board, at its meeting on 14th August 2024, approved your Research Proposal for the M.Sc. Degree entitled, *Credit Risk Management and Liquidity of Commercial Banks in Kenya*.

You may now proceed with your Data collection, subject to clearance with the Director General, National Commission for Science, Technology & Innovation and Ethics Review Committee, Kenyatta University.

As you embark on your data collection, please note that you will be required to submit to Graduate School completed Supervision Tracking and Progress Report Forms per semester. The Forms are available at the University's Website under Graduate School webpage downloads.

Also, please ensure that you publish article(s) from your thesis before submitting it to Graduate School for examination as per the Commission for University Education and Kenyatta University guidelines.

Thank you.

ANGELA KIMARU
FOR: EXECUTIVE DEAN, GRADUATE SCHOOL

CC. Chairman, Department of Accounting and Finance

Supervisors:

1. Dr. Daniel Makori
c/o Department of Accounting and Finance
Kenyatta University

2. Dr. Nancy Muchira
c/o Department of Accounting and Finance
Kenyatta University

Appendix III: NACOSTI Permit



REPUBLIC OF KENYA

NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION

Ref No: **319487**



NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION

Date of Issue: **11/October/2024**

RESEARCH LICENSE



This is to Certify that Mr. Warsame Mohamed Osman of Kenyatta University, has been licensed to conduct research as per the provision of the Science, Technology and Innovation Act, 2013 (Rev.2014) in Nairobi on the topic: CREDIT RISK MANAGEMENT AND LIQUIDITY OF COMMERCIAL BANKS IN KENYA for the period ending: 11/October/2025.

License No: **NACOSTIP/24/48888**

Applicant Identification Number: **319487**

Director General

NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION

Verification QR Code



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See overleaf for conditions

Appendix IV: Questionnaire

Kindly provide relevant answers to the following questions by way of tick.

SECTION A: GENERAL INFORMATION

1. Kindly specify your gender

Male Female

2. What is your highest level of education?

Certificate Diploma Undergraduate Degree Masters and above

3. Kindly indicate the number of years you have worked with this bank

Less than 5 years 6-10 years 10-15 years Over '15 years

SECTION B: CREDIT INFORMATION SHARING

4. Below are a number of aspects of credit information sharing. Kindly indicate the extent which your bank relies on them during the credit/loan appraisal process of its customers. Use a scale of 1-5 where 1-no extent, 2-little extent, 3-moderate extent, 4-large extent and 5-very large extent.

Credit Information Sharing	1	2	3	4	5
Credit scores of customers					
Internal credit reports					
Credit history of customers					
Credit reports from Credit Reference Bureaus (CRBs)					

SECTION C: LENDING REQUIREMENTS

5. To what extent does your bank rely on the following lending requirements when carrying out credit appraisal of customers to determine loan qualification. Use a scale of 1-5 where 1-no extent, 2-little extent, 3-moderate extent, 4-large extent and 5-very large extent.

Lending Requirements	1	2	3	4	5
National identification cards of the loan applicants					
Passport photographs					
Logbooks					
Land title deeds					

THANK YOU

Appendix V: Data Collection Sheet

Year	Total loan provision	Total loans	Total deposits	Political risk index
2018				
2019				
2020				
2021				
2022				

Appendix VI: List of Commercial Banks in Kenya

1. Equity Bank Kenya Ltd
2. KCB Bank Kenya Ltd
3. NCBA Bank Kenya Plc
4. Co-operative Bank of Kenya Ltd
5. ABSA Bank Kenya Plc
6. Diamond Trust Bank (K) Ltd
7. Stanbic Bank Kenya Ltd
8. Standard Chartered Bank (K) Ltd
9. I & M Bank Ltd.
10. Family Bank Ltd
11. National Bank of Kenya Ltd
12. Ecobank Kenya Ltd
13. Bank of Africa Kenya Ltd
14. Bank of Baroda Ltd
15. Prime Bank Ltd
16. Bank of India
17. Citibank N.A. Kenya
18. HFC Limited
19. Sidian Bank Limited
20. SBM Bank (Kenya) Ltd.
21. Kingdom Bank Limited
22. Access Bank (Kenya) PLC
23. Gulf African Bank Ltd
24. First Community Bank Ltd
25. Consolidated Bank of Kenya Ltd
26. Credit Bank Plc
27. African Banking Corporation Ltd
28. Spire Bank Limited
29. Guaranty Trust Bank (Kenya) Ltd
30. Guardian Bank Limited
31. Paramount Bank Ltd
32. UBA Kenya Bank Ltd
33. M-Oriental Bank Ltd
34. DIB Bank Kenya Ltd
35. Habib Bank A.G. Zurich
36. Middle East Bank Ltd
37. Victoria Commercial Bank Plc
38. Mayfair CIB Bank Ltd
39. Development Bank of Kenya Ltd