The Strategic JOURNAL of Business & Change MANAGEMENT

ISSN 2312-9492 (Online), ISSN 2414-8970 (Print)

www.strategicjournals.com

Volume 11, Issue 4, Article 027

CREDIT RISK AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KISII COUNTY

Bwogo Constance Chepkirui & Dr. Julius Miroga, PhD

The Strategic JOURNAL of Business & Change MANAGEMENT
ISSN: 2312-9492 www.strategicjournals.com
Vol. 11, Iss.3, pp 432 – 442, October 19, 2024. www.strategicjournals.com, © Strategic Journals

CREDIT RISK AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KISII COUNTY

Bwogo Constance Chepkirui [1] & Dr. Julius Miroga, PhD [2]

[1] Master Student, Jomo Kenyatta University of Agriculture and Technology, Kenya
[2] Lecturer, Jomo Kenyatta University of Agriculture and Technology, Kenya

Accepted: October 5, 2024

DOI: http://dx.doi.org/10.61426/sjbcm.v11i4.3096

ABSTRACT

The study focused on assessing the relationship between Credit Risk management practices and financial performance of commercial banks in Kisii County. The study was anchored on the theories namely; Agency theory, Interest rate parity theory and International Fischer's effect theory. The study was based on the objective of determine the influence of credit risk survey research design. The targeted population was on 21 commercial banks in Kisii County. The sample included the whole population since it was manageable. The Record survey sheet was used as an instrument of data collection. Piloting was done on the respondents from Kisumu County. The result indicated that Pearson Correlation coefficient was represented with a strong, positive relationship between Credit risk and financial performance of commercial banks in Kisii County, Kenya. Census technique was applied on all the targeted institutions. Descriptive and inferential analysis of the data for the study was analyzed by the use Statistical Package of Social Sciences (SPSS). Linear regressions will be used to show the relationship between the variables. The findings indicated that Credit Risk Management had a significant positive influence on Financial Performance. The study recommends the management of various Institutions to embrace the professional Credit Risk Management practices as there is an improvement in Finance Performance. The study recommends for further study using similar variables but different methodology.

Key Words: *Credit Risk, Risk Management Practices and Financial Performance*

CITATION: Bwogo, C. C., & Miroga, J. (2024). Credit risk and financial performance of commercial banks in Kisii County. *The Strategic Journal of Business & Change Management,* 11 (4), 432 – 442. http://dx.doi.Org/10.61426/Sjbcm.v11i4.3096

INTRODUCTION

According to Mwai (2023), they are financial intermediaries that primarily produce monetary money through the issuance of saving deposits, which are deposits that are receivable on demand, and time deposits, which are deposits with stringent maturity terms. Both of these types of deposits are referred to as deposits. There is a major contribution that commercial banks make to the expansion of the economy through the acquisition of stakes and the subsequent donation or lending of those stakes to business owners as seed money for their respective enterprises. Furthermore, commercial banks provide directly to the government the ability to lend money and also provide management experience to individuals who run small enterprises. When it comes to economic development, the activities made by local commercial banks are directly related to the outcomes of any state. In order for the banking business to successfully carry out its activities and continue doing so, it is vital for the industry to have high-quality financial execution. Nevertheless, avoiding such dangers is a challenging endeavor. Additionally, the financial performance of a bank and the prospects that it presents are interconnected, and it is required to do an analysis of both of these aspects simultaneously in order to evaluate whether or not the bank will continue to exist.

Commercial banks are forced to operate in circumstances that are filled with uncertainty and instability when it comes to carrying out their responsibilities. The amount of attention that has been paid to the performance of banks is a direct result of the competition that exists between firms and the globalization of the activities that they engage in. Businesses have been able to lower their costs as a result of this, which has enabled them to bring in a bigger number of new consumers and to maintain the clients they now have. On the other hand, the difficulty lies in determining the kind of stable liquidity situation that results in the maximum earnings. The banking industry has been going through a period of time that can be described as a financial crisis at a variety of different moments in time all around the world. The findings of Alqahtani et al. (2017) demonstrate that this demonstrates that no economy is immune to the threat of a financial crisis. There were a number of markets that experienced a pause in their growth. The return on equity (ROE) had a number of shifts during the course of the years 2017 through 2021. Return on equity (ROE) in Germany was 5.31 percent during the third quarter of 2021, while in France it was 9.3 percent, in Russia it was 15.7 percent, in the United States it was 5.31 percent, and in India it was 8.760 percent. In India, the ROE was 8.760 percent. These figures are derived from the return on equity (ROE) performance of commercial banks located all around the world. According to forecasts published by the European Commission, the gross domestic product of Germany is anticipated to experience a fall of 6.3 percent in the year 2020. Within the European Union, this translates to a decrease of 9.7 percent in the United Kingdom, 10.6 percent in France, 10.9 percent in Spain, 11.2 percent in Italy, and an overall decrease of 8.3 percent across the board.

According to Mwai (2023), commercial banks play a significant part in assisting society in the process of allocating limited resources to projects that would produce the greatest returns and in promoting the realistic allocation of risk among traders and investors. This is a function that commercial banks play in the process of supporting society. One of the factors that leads to the imbalance of financial power among banks is the fact that the global financial crisis brought to light the significance of bank regulation in the process of risk mitigation when it comes to the process of risk mitigation.

The authors Ndagara et al. (2020) suggest that in order to forestall the devaluation of the Kenyan currency, it is advised that each state establish a central bank that is accountable for the maintenance of economic stability through the management of inflation. Central banks ensure that

commercial banks are subject to the appropriate amount of regulation in order to protect the financial well-being of the general public and guarantee that they do not suffer financial losses. Because it is the only organization that is authorized to regulate banks, the Central Bank of Kenya (CBK) has the ability to exclude any bank that does not comply with its criteria. This is because it is the only body capable of regulating banks. When it comes to the stability of commercial banks, the efficacy of their management is directly linked to the quality of the management. According to one of the regulations that have been set by CBK, commercial banks are obligated to adhere to all effective systems of financial risk management. This is a requirement that has been imposed against them.

According to Drechsler et al. (2021), the phrase "interest rate risk" refers to the risk that arises as a result of variations in interest rates that have an effect on the assets and obligations of a firm. This risk can create a significant amount of uncertainty for the organization. The risk may also be characterized by referring to the possibility that the price of the asset may decline as a result of unanticipated changes in the interest rate. This is another aspect that can be used to identify the risk. One of the most significant risks associated with investing in fixed-rate bonds is the possibility of interest rate swings. In the context of finance, the term "credit risk" refers to the possibility that customers, who are also referred to as borrowers, might not satisfy their financial obligations by the time they reach maturity or the due date. Credit risk is defined by Isanzu (2017) as the threat that a debtor provides to the profitability of a company and, ultimately, its capital when the debtor fails to satisfy the conditions of a credit agreement with a financial institution for whom the firm has entered into a credit agreement.

The presence of moral hazards and adverse selection, both of which can be linked to the existence of asymmetric information, are the causes of risk that are present in the financial industry. The level of financial risk that is connected with an organization is a crucial factor in determining the profitability of financial institutions. This is because a significant portion of the money that these institutions generate comes from loans that carry interest. The effectiveness of institutions, on the other hand, is influenced by the financial risk they face. In light of this, it is of the utmost importance to implement suitable risk management (Bhattarai, 2016). Risk has been shown to be a valid measure of the efficacy of financial institutions within the field of finance, according to research that was conducted in the past. An illustration of this may be observed in the case of non-performing loans (NPL), which acts as a proxy for credit risk and has the ability to disrupt the overall credit system of a bank, hence reducing the value of the bank (Afriyie & Akotey, 2012).

In their research, Felix and Claudine (2008) investigated whether or not there is a connection between credit risk management and the performance of banks in Sweden. It is possible to draw the conclusion, on the basis of their data, that there is an inverse link between return on equity (ROE) and return on assets (ROA), both of which are indices of profitability, and the percentage of non-performing loans to total loans in financial institutions. Consequently, the profitability of the business suffers as a consequence of this relationship.

According to Owojori et al. (2011), who conducted a study on the topic of risk management in Nigerian banks during the post-consolidation era, the data obtained from the liquidated banks provided clear evidence that the failure to recover loans and advances given to customers, as well as to directors or companies associated with directors/managers, significantly contributed to the financial distress that these banks experienced. This was emphasized in their study. A considerable number of banks, namely sixty out of the one hundred and fifty banks that were operational at the time, were in a state of distress during the height of the financial crisis in the year 1995. In this particular period of time, the financially troubled banks displayed a ratio of non-

performing loans and leases to total loans and leases that was 67%. In 1997, the ratio was 82%, which was a significant decrease from the previous year's 79%. After that, by the end of the year 2002, the licenses of thirty-five of the institutions that were experiencing financial difficulties had been revoked. The year 2003 marked the year that a single financial institution, specifically Peak Merchant Bank, went out of business. In the year 2004, there was not a single bank that went out of business. As a result, the number of banking licenses that the Central Bank of Nigeria (CBN) has revoked since 1994 remained at 36 until January of 2006. A total of fourteen other banks had their licenses revoked at that time because they were unable to comply with the minimum re-capitalization directive issued by the Central Bank of Nigeria (CBN). During the time period in question, the banking licenses were revoked, and it was discovered that a number of financial institutions had performing credit ratios that were lower than 10% of their total loan portfolios. The percentage of non-performing loans to total loans within the industry witnessed an improvement in the year 2000, reaching 21.5%. This was a significant improvement. In the years that followed, by the time the year 2001 came to a close, this ratio had dropped to 16.9%. The proportion fell to 21.27% in 2002, climbed to 21.59% in 2003, and reached 23.08% in 2004 according to the Annual Reports distributed by the National Deposit Insurance Corporation (NDIC) for a number of years.

One of the primary focuses of the investigation that Olawale L. S. (2015) carried out was to investigate the influence that credit risk has on the overall performance of commercial banks in Nigeria. The unfavorable effects that categorized assets have on the capitalization of banks served as the impetus for the study. In order to demonstrate the factual information that is associated with the scenario, the utilization of a secondary data source was utilized instead. An assortment of sources, such as annual reports, relevant literature, and the statistics Bulletin released by the Central Bank of Nigeria (CBN), were utilized in order to gather the secondary data. According to the data, there is a negative link between the ratio of loans and advances to total deposits and profitability; however, this association does not meet the criteria for statistical significance at a level of significance of 5%. Furthermore, the findings indicate that there is a negative association between the ratio of non-performing loans to loans and advances and profitability, which is statistically significant at a 5% level of significance. This relationship is supported by the fact that the ratio is negative. The findings of this study indicate that there is a significant association between the performance of banks, notably in terms of profitability, and the management of credit risk, specifically in terms of loan performance. There are a number of important aspects to consider when evaluating the asset quality of a financial institution, including loans and advances, as well as loans that are not being repaid. Several recommendations were made as a result of the study, one of which was that management should be cautious while developing a credit policy in order to prevent any negative influence on profitability. Additionally, it stressed the significance of knowing how credit policy effects bank operations in order to guarantee the responsible utilization of deposits and the maximization of profits. This was done in order to ensure that this was accomplished. Inadequate credit risk management has a significant impact on the profitability of banks, affects the quality of their assets, and amplifies the occurrence of loan losses and non-performing loans, potentially terminating in financial difficulty. A systematic evaluation of the lending practices of financial institutions for the sake of policy should be carried out by the Central Bank of Nigeria (CBN) in order to solve this issue. In order to evaluate the severity of the credit crunch, one possible way entails differentiating the influence of loan supply from the influence of loan demand, while also taking into consideration the viewpoints of businesses on the lending behavior of banks or financial institutions. In the end, the improvement of the securities market will result in

good repercussions for the overall progression of the banking sector. This will be accomplished through the enhancement of competitiveness within the financial sphere.

The objective of the research carried out by Kargi (2011), which was subsequently mentioned by Kolapo et al. (2012), was to evaluate the impact that credit risk has on the financial performance of banks with operations in Nigeria. The annual reports and accounts of a number of different banks were analyzed in order to provide the financial ratios that were acquired for the years 2004 through 2008. Following that, these ratios were subjected to analysis using descriptive, correlational, and regression methods in order to evaluate the performance of the bank as well as the credit risk. According to the findings of the research, the management of credit risk has a significant impact on the extent to which banks in Nigeria are able to deliver satisfactory financial outcomes. Based on the findings of the research, it can be concluded that there exists a negative correlation between the profitability of banks and the levels of loans and advances, non-performing loans, and deposits. It may be deduced from this that larger levels of these characteristics can potentially enhance the risk of illiquidity and financial difficulty for financial institutions.

In a case study that was carried out by Kayogire and Shukla (2016), an investigation was carried out to assess the effect that Equity Bank (Rwanda)'s credit risk management policy had on the bank's overall financial performance. The findings of the study demonstrated that there is a noticeable connection between the financial performance of the bank and the collectability of its loans, as well as the effectiveness of the lending evaluation criteria that the bank has put into place. The primary data was collected from a sample of 57 credit officers who were employed by the bank. In a study that was carried out by Kibui (2014), the researcher investigated the influence that credit risk management practices had on the financial performance of Harambee Sacco. The primary objective of the study was to investigate the influence that client appraisal methods, credit policy development, existing credit risk monitoring and control methods, as well as systematic defaulter follow-up and loan defaulter reports, have on the financial performance of Savings and Credit Cooperative Organizations (SACCOs). Descriptive research was the approach that was employed for this investigation. The researcher chose 58 individuals to participate in the study as a representative sample from the whole population of 178 credit officers who were the focus of the investigation. In this particular conversation, we will be talking about Harambee SACCO, which is situated in Nairobi. Using a straightforward random sample method, the researchers collected their data. According to the findings of the research, Sacco utilized a number of risk mitigation strategies in the management of credit risk. These strategies included the utilization of guarantors, collaterization, shareholding, and insurance respectively. In addition, the research demonstrated that the introduction of credit risk management results in a considerable improvement in the performance of Savings and Credit Cooperative Organizations (Saccos). Additionally, the findings of the investigation demonstrated the presence of a specialized computerized reporting system that permits the timely detection of loans that have fallen behind on their payments.

In a study that was carried out by Ndegwa (2017), the author investigated the influence that credit risk has on the financial performance of commercial banks that are listed on the Nairobi Securities Exchange. Through the course of the research, a specific investigation of the influence of credit risk on return on equity as well as return on assets was carried out. Utilizing secondary data obtained from the financial statements of eleven different commercial banks, a descriptive research design was utilized in order to conduct an investigation of a sample of eleven different banks. For the period of time spanning from 2016 to 2020, the financial statements of the particular bank were readily

available on the official website of the bank. Analytical methods such as descriptive analysis, correlation analysis, and regression analysis were utilized by the researchers in order to determine the relationship between the variables. Both Return on Assets (ROA) and Return on Equity (ROE) were found to have a negative and weakly positive association with the Capital Adequacy Ratio, according to the findings of the study. Based on the findings of the study, it was discovered that the financial performance of these banks was positively impacted by a variety of parameters, including capital sufficiency and the ratio of loans to deposits, among other aspects. According to the findings of the research, credit risk tends to have an effect on the financial performance of commercial banks that are listed on the National Stock Exchange (NSE).

Statement of the Problem

In Kisii County, According to CBK's 2020 report, the performance of commercial banks has been continuously declining over the course of time. From what we can tell, the return on equity (ROE) of these financial institutions was 24.4% in 2016 and 23.6% in 2017. Furthermore, the decline reached 22.5% in 2018, 21.8% in 2019, and 13.9% in 2020. This represents a significant increase. It is a clear indication that the return on equity (ROE) growth has been decreasing, which implies that the financial performance has been uniformly worse across the chosen time periods. In recent years, businesses have made an effort to provide an explanation for the poor performance of these organizations. With that being said, it has not been a simple undertaking. It is therefore necessary for financial institutions to take into account both the macro and the micro environmental demands in order for them to be successful (Chidozie & Ayadi, 2017).

Empirical research has been conducted in the past on a number of different areas of bank financial risk and performance, and the results of these studies have been inconsistent. The researchers Maniagi (2018), Abdulrehman and Nyamute (2018), Hoque et al. (2020), Gikombo and Mbugua (2018), Juma and Atheru (2018), Mabati and Onserio (2020), Muriithi (2016), Charmler et al. (2018), Maniagi (2018), Isanzu (2017), Ndalu (2018), and Paul and Musiega (2020) all make use of empirical data in their research on the financial risk and performance of banks. Findings of the research conducted by Abdulrehman and Nyamute (2018) indicate that commercial banks fared significantly better. Credit risk has a detrimental effect on the profitability of commercial banks. Conclusions that are contradictory have been reached as a result of exhaustive research into the connection between financial risks and financial success. While some studies discovered a connection between taking risks and achieving financial success, others discovered that the connection was either weak or nonexistent (both in a positive and negative sense). An alternate method of operationalizing financial risk was utilized by the researchers, and a number of the conclusions or studies are focused on states that are not Kenya. This research therefore focused on investigating the relationship between Credit risk management practices and financial performance of commercial banks in Kisii County.

Study objective

To determine the influence of credit risk on financial performance of commercial banks in Kisii County.

Research Question

What is the influence of credit risk on financial performance of commercial banks in Kisii County?

LITERATURE REVIEW

Theoretical Literature Review

Agency Theory

It was Jensen and Meckling (1976) who first developed the concept of "agency," which Tekin and Polat (2020) define as a method for resolving and clarifying issues between principals and agents. Through the avoidance of agency conflicts between the principal and the agents, the strategy with the goal of increasing shareholder value is being

implemented. The fact that there is a clear or direct connection between the performance of an organization and the outcomes of its finances is demonstrated by the hypothesis. The agreement that is reached between the owners of production-related assets and the agents is what Jensen and Meckling believe to be the determining factor in the industry. Knowledge inequality creates a barrier for the principal-agent relationship to function properly. The enhancement of the flow of information facilitates the establishment of a balance between the competing objectives of the parties. This is the primary hypothesis the study is based on. The fact that the expenses of the agency are reduced after the owner's criteria are satisfied makes this concept pertinent to the research that I am conducting. Commercial banks are the subject of this investigation, and the board of directors is responsible for acting in a manner that is beneficial to the shareholders. Nevertheless, it is possible that they do not always act in the best interests of shareholders who are looking to increase their wealth.

Interest Rate Parity Theory (IPT)

Keynes first put up the idea in the year 1923. According to this theory, fluctuations in the minimum interest rate are brought about by differences in interest rates that exist between countries that engage in commerce. Additionally, interest rate parity is the relationship between interest rates and currency rates that indicates how they are related to one another. According to Ismailov and Rossi (2018), the forward rate can be determined by first multiplying the spot exchange rate by the interest rate in the home country, and then dividing the result by the interest rate in the country that is the target of the relationship. An knowledge of interest rate parity, which is an essential subject in the banking industry, is provided by Interest Rate Parity Tax. The fact that this theory is connected to concerns concerning interest rates, which are essential to the functioning of banks, makes it pertinent to the research that I am conducting. Using this method makes it easier to calculate the interest rates that banks charge for loans and other financial services. According to this line of reasoning, increased earnings result in enhanced financial soundness of commercial banks as well as rates of interest that are higher.

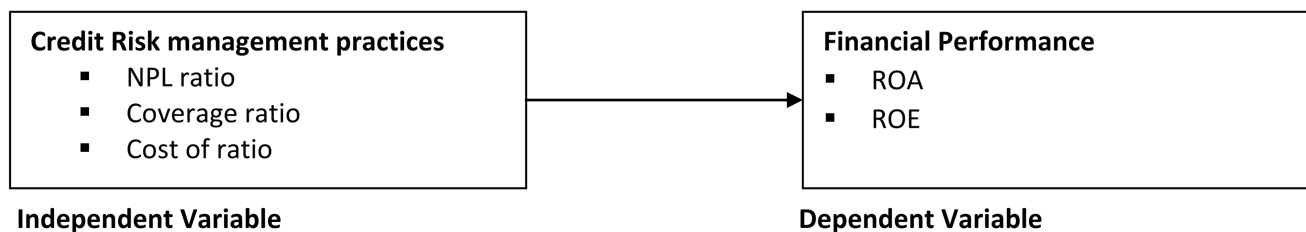
International Fischer’s Effect Theory (Irving Fisher 1930)

Irving Fisher first put out this idea in 1930, and it was subsequently published in his book which was titled The Theory of International Fishers Effect. He claimed that there is a connection between interest rates and currency rates that cannot be severed. The genuine rate of interest is the same across all nations, according to the theory, since capital movements generate opportunities for arbitrage between companies or financial institutions. This ensures that the true rate of interest is consistent. This suggests that countries with lower interest rates also have lower inflation, and vice versa on the other hand. However, this suggests that the actual currency of the country will decrease in value over the course of time. The concept is relevant to the financial sector because of the fluctuation in the demand and supply of currency, which leads to a change in price and, as a consequence, an exchange rate. According to Mabati and Onserio (2020), the concept is connected to the risk of fluctuations in foreign currency rates, which has a substantial influence on commercial banks in Kenya. During the process of determining variations in exchange rates, the technique takes into consideration the market interest rate, but it does not take into account the cost of inflation.

Currency exchange rates reveal interest rate vulnerabilities in the form of risk-free instruments derived from a number of different currency alternatives. Over the course of time, it is anticipated that the value of a nation's currency will increase if interest rates in the current market are high. In accordance with the findings of Kalemli-Ozcan and Varela (2019), the presence of a high nominal rate results in the depreciation of foreign currency due to the anticipation of even higher inflation rates. Firms are able to reduce the financial

risk that is involved with currency exchanges by utilizing forward contracts, which are arranged through commercial banks. These contracts allow firms to lock in exchange rates for the foreseeable future. The significance of the relationship between the nominal interest rate and the current inflation rate, as well as the impact of these two variables on the financial performance of commercial banks, is demonstrated by this hypothesis that is related to education.

Conceptual Framework



Independent Variable **Dependent Variable**

Figure 1: Conceptual Framework

METHODOLOGY

Research Design: According to Gujarati (2007), a research design is a comprehensive master plan of the research study that is going to be carried out. This plan provides an overarching description of the procedures that are going to be utilized in order to ensure that the necessary data is collected in an appropriate and cost-effective manner in relation to the subject matter that is currently being investigated. There was a descriptive survey research design utilized for the investigation.

Target Population: According to Tiwari, Arya, and Bansal (2017), the term "population" has been defined as "the collection of components for study use." A connection must to exist between the people who take part in the research and the objectives of the study, as stated by Daniel (2016). The research focused on 21 commercial banks that were active in Kisii County, which is located in Kenya.

Sample and Sampling Technique: As a complete method for picking a group that is representative of a target population, sampling is an approach that is used. In addition to this, it places an emphasis on the approach that the researcher utilized in order to select the components that were included in a study, which ought to be dependable and acceptable (Kothari, 2004). Every single one of Kisii County's twenty-one commercial banks participated in the study. According to Cooper and Schindler (2006), a census analysis is feasible in situations when the research population is very small and the components are considerably different from one another.

Research Instrument: Data collection, as defined by Creswell (2002), is the process of collecting information from a representative sample of the participants who participated in a study. "Data collection" is the word that is used to describe the procedure that researchers go through in order to gather information from the people who are participating in their study. "Data extraction methods" (Axinn & Pearce, 2006) is the phrase that is used to describe the procedures that are utilized in order to collect the information that is required in order to carry out the study. For the purpose of collecting secondary data, a specialized data collection sheet was utilized. From sources that are accessible to the general public, such as annual reports and financial statements, each and every variable for the study was retrieved.

Data Analysis: The collected data was thoroughly examined and checked for errors and tabulated accordingly. The study used descriptive statistics to analyse the data to establish patterns, trends and relationships. Data was presented in frequency tables. The effect of Credit Risk Management practices on Financial Performance. The applicable regression model is shown below:

$y = \alpha + \beta_1 X_1 + \varepsilon$

Where;
Y= Financial Performance
α =constant
β_1 = parameter estimate
X_1 = Credit Risk Management practices
ε is the error of prediction.

FINDINGS AND DISCUSSION

Response Rate

The study involved all the 21 Commercial Banks operating in Kisii County. A census analysis is viable when the research population is small and the components are fairly varied from one another (Cooper & Schindler, 2006).

Descriptive Statistics for Credit Risk Management practices

These are summarized responses on whether Credit Risk Management Practices influence performance of banking institutions in Kisii.

Inferential statistics

Correlation Analysis

The correlation analysis presented in Table 1 focuses on the relationship between employee performance and several key variables, including job rotation, coaching and mentoring, job shadowing, and employee orientation. The findings reveal significant correlations that highlight how these constructs may correlate with employee performance.

Table 1: Correlation Analysis

		Credit Risk Practices	Financial Performance
Credit Risk Practices	Pearson Correlation	1	
	Sig. (2-tailed)		
	N	92	
Financial Performance	Pearson Correlation	.529**	1
	Sig. (2-tailed)	.000	
	N	92	92

Findings showed that there is a strong positive correlation between financial performance and Credit Risk Assessment, with a Pearson correlation coefficient of 0.529 ($p < 0.01$). This suggests that higher levels of Credit risk management practices are associated with improved performance, indicating that effective support and guidance can significantly enhance performance.

Analysis of linear regression;

Linear influence of Risk Assessment on performance

This tested the direct influence Risk Assessment on performance. The results were shown in table 2. Regression analysis was used to determine the relationship between the independent or predictor variables and a dependent variable.

Linear influence of Credit Risk Management practices on financial performance

This tested the direct influence Credit Risk Management on financial performance. The results are shown in table. Regression analysis was used to determine the relationship between the independent or predictor variables and a dependent variable.

Table 2: Direct influence of Credit Risk Management Practices on financial Performance

R	R Square	Adjusted R Square	Std. Error of the Estimate
0.79	0.6241	0.6134	0.0041

Regression model summary in Table 2 had an Adjusted R-square of 0.6134 that indicates that

61.34 percent of changes in financial performance of commercial banks are explained by Credit Risk Performance, while extraneous factors accounted for 38.66 percent.

$y = 2.516 + \mathbf{0.509X_2}$

Where;

y = Performance

X_2 = Credit Risk Management Practices

CONCLUSIONS AND RECOMMENDATIONS

The objective sought to determine the influence of credit risk on financial performance of commercial banks in Kisii County. The result indicated that Pearson Correlation coefficient which represented an average, positive relationship between credit risk and financial performance of commercial banks in Kisii County, Kenya.

The research question focused on as to whether the credit risk influences financial performance of commercial banks in Kisii County. The study concluded that a unit increase in credit risk results to an increase in financial performance of commercial banks in Kisii County.

It is recommended that the management of Kenyan commercial banks learn more about credit analysis and loan administration in order to increase their proficiency. The establishment of stringent credit laws and lending standards is an absolute necessity. Additionally, management is expected to guarantee that the terms and conditions of loan approvals are adhered to when making decisions. As a consequence of this, lending criteria need to be approved by senior management and disseminated to every member of the team. Because of this, losses from nonperforming loans will be reduced, and asset quality management will be improved; as a result, banks' expenditures will increase, which will ultimately lead to an increase in profits. The ratio of loans and advances to total deposits should be evaluated on a regular basis by the bank because it has an effect on the profitability of the institution. According to the idea of financial distress, credit risk is one of the factors that contributes to financial distress, which can result in a decreasing rate of return on shareholders' equity.

Areas for further studies

Similar study can be done on other studies using similar variables, though using different methods.

REFERENCES

Abdulrehman, A. A., & Nyamute, W. (2018). Effect of mortgage financing on financial performance of commercial banks in Kenya. *Journal of International Business, Innovation and Strategic Management*, *2*(2), 91-122.

Abdulrehman, A. A., & Nyamute, W. (2018). Effect of mortgage financing on financial performance of commercial banks in Kenya. *Journal of International Business, Innovation and Strategic Management*, *2*(2), 91-122.

Chidozie, U. E., & Ayadi, F. S. (2017). Macroeconomy and banks' profitability in Nigeria. *African Research Review*, *11*(2), 121-137.

Chipeta, C., & Muthinja, M. M. (2018). Financial innovations and bank performance in Kenya: Evidence from branchless banking models. *South African Journal of Economic and Management Sciences*, *21*(1), 1-11.

Drechsler, I., Savov, A., & Schnabl, P. (2021). Banking on deposits: Maturity transformation without interest rate risk. *The Journal of Finance*, *76*(3), 1091-1143.

Gikombo, E. M., & Mbugua, D. (2018). Effect of select macro-economic variables on performance of listed commercial banks in Kenya. *International Academic Journal of Economics and Finance*, *3*(1), 80-109.

Isanzu, J. S. (2017). The impact of credit risk on financial performance of Chinese banks. *Journal of International Business Research and Marketing*, *2*(3).

Juma, A. M., & Atheru, G. (2018). Financial Risks Analysis and Performance of Commercial Banks in Kenya. *Journal of Finance and Accounting*, *2*(2), 76-95.

Juma, A. M., & Atheru, G. (2018). Financial Risks Analysis and Performance of Commercial Banks in Kenya. *Journal of Finance and Accounting*, *2*(2), 76-95.

Mabati, J. R., & Onserio, R. F. (2020). The Effect of Central Bank Rate on Financial Performance of Commercial Banks in Kenya. *J. Financ. Account*, *4*, 25-40.

Maniagi, G. M. (2018). *Influence of financial risk on financial performance of commercial banks in Kenya* (Doctoral dissertation, JKUAT).

Mwai, D. K., & Ragui, M. (2023). Internal Audit and Business Resilience in Power Sector. A Case of Geothermal Development Company. *Journal of Strategic Management*, *7*(2), 50-71.

Ndagara, M. M., Mugendi, L. K., & Galo, N. M. (2020). Effectiveness of Monetary Policy Intervention on Exchange Rate Volatility in Kenya.

Nzuve, R. M. (2016). *Impact of macroeconomic factors on financial performance of deposit-taking micro finance institutions in Kenya* (Doctoral dissertation).

Oyewo, B. (2022). Enterprise risk management and sustainability of banks performance. *Journal of Accounting in Emerging Economies*, *12*(2), 318-344.