

ABSTRACT

The study is set to gain an understanding of the effect of interest rate capping on the performance of banks in Kenya, a case of Kisumu County. There is an existent relationship between interest rates and the performance of banks, which has been an area of interest for academia for a number of decades world over. With the focus on how performance of commercial banks is affected by interest rate capping, the specific objectives of the study will include; assess the effect of interest rate capping on customers borrowing in commercial banks in Kisumu County, Kenya; examine the effect of interest capping on inflation rates in Kisumu County, Kenya; and determine the effect of interest capping on discount rates in Kisumu County, Kenya. The study will be based on the theories of interest rates by Keynes (1936), Caplan (2000) and Friedman, (1991) who argue that savings are hinged on interest rates and the demand for capital by customers arising from investment decisions based on saving. The study adopted a cross-sectional study design in which 34 commercial banks operating in Kisumu County were targeted. Both primary and secondary data were collected. The primary data was collected using self-administered questionnaires which were distributed to staff and top managers of the selected commercial banks. The data collected was analysed descriptively to give a summary of the data characteristics while inferential statistics was used to establish associations and relationships between variables. Regression analysis was used to establish relationships between borrowing, inflation rates, discount rates, and the overall performance of commercial banks in Kisumu County Kenya. Findings emanating from this study are useful in understanding the effect of interest rate capping on performance of financial institutions particularly the local commercial banks and can aid the Kenyan policy makers to carefully plan and forecast the impact of such moves with a view of ensuring that while local commercial banks thrive in their mandate, the customers are also safeguarded and satisfied by the services received from the banks. The study set the interest rate cap coefficient of multiple regressions at $r^2 = 0.585$ with an influence scale equated at $p < 0.001$, which gives the implication that there is a positive correlation between commercial banks financial, with the interest rate cap affecting their performance at a percentage of 58.5%. A response mean score of 2.810, 3.87833, 3.92333 in terms of consumer borrowing, inflation and discount rates respectively, indicating that the respondents had a moderate extent to agree with the questions on each of the three variables requirement. The regression model also gives the connotation that holding the dependent variables constant there would be an achievement of 1.932 in form of commercial banks in Kisumu county financial performances. A unit increase in each of the variables would result in a development of the commercial banks' performance by factors of -0.071, -0.257 and 0.611 in terms of consumer borrowing, inflation and discount rates respectively. The study therefore recommended that in order for the commercial banks within Kisumu County to ensure a stable and improved performance, there is need for stability or an improvement in the interest rate levels.