ABSTRACT

The Kenyan banking sector is categorized into three tiers, tier I, II and III based on bank size. The profitability of tier II and III has been declining begging the question as to whether the size of the bank has any influence on the performance of the banks. This study determines the influence of internal equity capital on the financial performance of lower-tier commercial banks in Kenya. The study employed a descriptive and explanatory research design. The study population was 26 commercial banks in Tier II and III commercial banks in Kenya from 2016 to 2020. The average internal equity for lower-tier commercial banks in Kenya was .364 in 2016 and .400 in 2017. In 2018, the internal equity sharply rose to 8.299, which was followed by a small decline to 7.782 in 2019 signifying that in 2018 and 2019, lower-tier commercial banks in Kenya employed more internal equity financing to finance their operations. Through the hierarchical regression, it was established that internal equity has a positive and significant influence on the financial performance of lower-tier commercial banks in Kenya. Bank size does not moderate the effect of internal equity on the net profit margin of lower-tier commercial banks in Kenya ($p = .202 > 0.05$; R2 change of 0.07). The study recommends that lower tier commercial banks need to encourage its shareholders to re-invest back their earnings rather than consuming them as dividends as internal equity is affordable and readily available when the bank is in urgent financial need.