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**DUPLICITY IN REGULATION AND PERFORMANCE OF THE
FINANCIAL SECTOR IN KENYA**

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Abstract

Purpose: The objective of the study was to investigate the duplicity in regulation and performance of the financial sector in Kenya. The specific objectives were; to review and identify regulation duplication/competition in existing regulatory framework for the financial sector in Kenya; to describe how regulatory effectiveness has been measured in empirical literature; to assess whether the current regulatory structure has affected the performance of the financial sector in Kenya and lastly to suggest potential ways of enhancing regulatory effectiveness in Kenya.

Methodology: The paper used a desk study review methodology where relevant empirical literature was reviewed to identify main themes and to extract knowledge gaps.

Findings: The study found out that financial sector in Kenya and other developing economies have reported losses on a large scale due to under regulation and regulator duplicity. Some of these have become insolvent, or have had to be taken over or rescued by their governments. A single market regulator clearly has its own advantages over multiple regulators. But it is more suitable for well-developed and mature markets which are smaller in size, like the UK. The study also found out that Kenya's economy and political arena are not mature enough to handle a single financial market regulator. In this light it can be asserted that even mature economies such as the United States still have multiple regulators.

Unique contribution to theory, practice and policy: Adherence to principles of open government, including transparency and participation in the regulatory process to ensure that regulation serves the public interest and is informed by the legitimate needs of those interested in and affected by regulation. Governments should ensure that regulations are comprehensible and clear and that parties can easily understand their rights and obligations. Organizations should create personalized technology systems that create a demand adaptation of ICT at every level of the organizational operations

Keywords: *regulations duplicity, financial performance, regulatory effectiveness, regulation structure*

INTRODUCTION

1.1 Background of the Study

The financial system has been undergoing the process of deregulation in certain western nations since the 1980s, with their governments either eliminating the government controls regulating financial institutions (Kumbhakar, Lozano-Vivas, KnoxLovell & Hassan 2005). It is because decision makers are persuaded that liberalization is the only method in which they can significantly raise these institutions' productivity and effectiveness. These initiatives aim to increase competition from banks over prices, products and territorial competition.

Financial regulations are the laws the state has enacted to control financial firms, Agborndakaw (2010). According to Agborndakaw (2010), these regulations seek to preserve orderly markets, authorize financial service providers, enforce relevant laws and prosecute market manipulation cases, protect clients and investors and promote financial system stability. Both policy authorities and foreign organizations implement these legislation.

Nevertheless, this de-regulation mechanism has led to mixed outcomes. For example, the Norwegian banks' deregulation allowed them to set their private lending rates as well as the amount of money they could lend out. The findings were very favorable to them though this was not the situation in India and the United states. According to Gudmundsson *et al.*, (2013), The Cooke Commission formulated two ideas in 1979, namely micro regulatory policy and macro regulatory policy.

One of the facets of the topic when considering regulation of financial institutions is the regulatory structure. The regulatory structure varies from state to state but the nature of the sector and the rationale for regulating it remains the same. There has been a lot of discussion in the recent past on the systemic dimension of legislation, which is what the regulatory agencies will take (Klomp & de Haan, 2011). The biggest issue was whether the financial markets should have a single or several regulators. Various countries addressed the topic differently. Some countries have thus adopted the model of the single regulator while others have adopted the model of the multiple regulators. The justifications for a single regulator include improving coordination, market integration, reducing transaction costs because of economies of scale, leading to better knowledge system and management sharing and mitigating systemic risks (Blejer, 2006). Several other countries have followed the model where a separate entity operates for each of the major sectors, namely finance, insurance, securities, and pension services, such as India and Kenya.

Historically Kenya's financial system have been subdivided along sector specific department. Therefore, a banking industry, an insurance industry and, more importantly, the capital markets and the social benefits sector have arisen. Other financial sector segments that however play a comparatively minor role in the formal sector are construction societies and organizations of microfinance (Agborndakaw, 2010). Financial markets in Kenya fell under what is commonly called emerging markets. Those are markets which are still in the process of development but which experience fast growth rates. Such markets contrast with the financial markets in developed countries such as the United States, which are highly competitive but rising slower (Gudmundsson, 2013). The financial industry is governed by the Central Bank and the controlling legislation is the

Banking Act, Cap 488 of Kenya 's Laws. The insurance market is governed by the Insurance Commissioner, and the controlling law is the Cap 487 Insurance Act. The investment sector is governed by the Capital Markets Authority and the governing legislation is the Capital Markets Act, Cap 485A. Kenya's central bank is the financial industry 's principal supervisor. It is the Central Bank that is required to control and oversee banks and other financial institutions, and mortgages finance firms, and generally ensure compliance with the statement of the Banking Act (Otieno, 2012).

Financial system operations can have a critical effect on economic development and economic stability and prosperity (Kumbhakar, 2009). It influences long-term economic growth by impacting the efficiency of intermediation between lenders and final borrowers of funds; by enabling consumers of external funds to be tracked, thereby influencing the productivity of capital enrolled; and by its implication for the amount of savings that will influence potential revenue-generating capacity of the economy (Klomp & de Haan, 2011). As a result of the high degree of leverage of its operations and its central position in settling all activities in the economy, it influences the stability of the economy, and any instability in one segment threatens affecting the stability of the entire system. The effect of the financial structures on growth has been empirically well founded (Gudmundsson, 2013). Given the complexity of explicitly measuring performance in the financial sector, large numbers of empirical studies have focused on size or structure measures that provide evidence of a correlation between the structure of the financial system and economic development (Levine et al., 2008).

Historically Kenya's regulatory framework has been structured along sectoral lines, with each sector having its own regulator (Blejer, 2006). Many countries generally followed this pattern. Nonetheless, in recent times, several countries have modified and continue to amend their regulatory structures in a bid to contend with developments in their banking systems (markets) and innovations within financial firms, notably sustainability of services provided by financial institutions, consolidation in the financial system, conglomeration of organizations to form one-stop financial firms (Otieno, 2012).

Barth, Caprio and Levine (2009) argue that all governments tend to regulate and control banks in order to ensure their economies remain stable. The purpose of this regulation is to protect the public good, especially consumer interest in the financial services which is the regulator's ultimate accolade (Blejer, 2006). This is in fact partly due to the introduction of regulations that do not have a contractual arrangement with the bank's or institution's director, which already illustrates the reason that the agents still have trust in the business. In the same way, Klomp and de Haan (2011) argue that financial industry specificities and peculiarities strengthen the need for financial regulation. In addition, regulation functions as a depositor security and risk management framework through the principal deposit guarantee structures and the last techniques of the lender. It also allows for the reconciliation of the agency's problems, the restraint of the leader's behavior patterns to act in the interest of the investors. Within the same viewpoint, Barth et al, (2008) consider the three big dysfunctions are forcing the state to intervene to effectively increase the financial market's yield.

This is the case of market imperfections, the reality of macro- and micro-level environmental impacts. As a consequence, financial regulation is required to control market practices which could

damage the public interest. According to Agborndakaw (2010), the purpose of banking regulation is to protect consumers from economic problems. The Basel Committee has not stopped to incorporate rules on effective governance and financial regulations in order to make sure the public interest and ensure effective functioning of these financial institutions, with the goal of maintaining the reliability and stability of the banking and financial system. In an international environment, this Committee sets guidelines for supervising the financial sector.

Nonetheless, amid this stringent prudential regulation, the progression of crises that have arisen has forced the members of the 20 (G20) community countries into adopting a new Basel III international solvency principle. Nonetheless, the Basel III agreement announced on December 16, 2010 was aimed at consolidating the banks following the global financial crisis of 2007, which triggered many bankruptcies (Otieno, 2012). This Agreement complements the Basel II Agreement. Yes, it includes taking some steps to improve internal control and restore effective governance laws, while increasing information transparency and enhancing bank risk mitigation

Financial regulation systems protect the banks against the economic and financial stress fluctuations that occur. This arrangement also reflects the quality and quantity of capital elements, the financial leverage, regular liquidity and enhanced disclosures. At the other side, the Basel III agreement characterizes the duties of the supervisory board in charge of supervising the role of external audit in banks. Establishing dialog between the regulatory supervisors and the external auditors is crucial.

Financial regulations can be assessed by looking at development in the financial sector, according to an OXERA report of September 2006, and this is achieved by attributing financial performance before proposed laws come into effect and the performance after. They are also assessed using assessments which show improvement in market outcomes resulting from regulation. It can also be used to make international comparisons to evaluate findings that are comparable in various countries (Blejer, 2006).

The primary objective of financial market regulation is the pursuit of macroeconomic and microeconomic stability. When a system is safeguarded this translates into macro controls over the financial exchanges, clearing houses and securities settlement systems. Measures pertaining to the micro stability of the intermediaries can be subdivided into two categories: general rules on the stability of all business enterprises and entrepreneurial activities, such as the legally required amount of capital, borrowing limits and integrity requirements; and more specific rules due to the special nature of financial intermediation, such as risk based capital ratios, limits to portfolio investments and the regulation of off-balance sheet activities (Otieno, 2012). The second objective of financial market regulation is transparency in the market, intermediaries and investor protection. This is linked to the more general objective of equity in the distribution of the available resources and may be mapped into the search for "equity in the distribution of information as a precious good" among operators (Klomp & de Haan, 2011).

At the macro level, transparency rules impose equal treatment regarding takeovers and public offers and the correct dissemination of information (insider trading, manipulation and, more generally, the rules dealing with exchanges microstructure and price-discovery mechanisms). At

the micro level, such rules aim at non-discrimination in relationships among intermediaries and different customers (conduct of business rules). The third objective of financial market regulation, linked with the general objective of efficiency, is the safeguarding and promotion of competition in the financial intermediation sector. This requires rules for control over the structure of competition in the markets and, at the micro level, regulations in the matter of concentrations, cartels and abuse of dominant positions.

It is commonly understood that financial regulation should be designed to achieve certain key policy goals, including: (a) safety and soundness of financial institutions, (b) mitigation of systemic risk, c) fairness and efficiency of markets, and (d) the protection of customers and investors (Otieno, 2012). These broad goals, while clearly important, do not take into account an additional factor that has come to be regarded as critical in any well-functioning regulatory system; namely, minimum regulatory burden through efficiency and cost-effectiveness. It is fair to say that each of the four models of financial supervisions designed to achieve the policy goals of regulation, albeit in different ways. The differences in the models may be more acute when viewed through the prism of regulatory burden, that is, efficiency and cost-effectiveness. Otieno (2012) states that, above all, regulatory structure has an impact on the overall effectiveness of regulation and supervision because of the expertise, experience, and culture that develops within particular regulatory agencies. Other major considerations when determining the appropriate regulatory structure include effectiveness in handling conflicts, the different costs of structures, and the issue of overlaps (unnecessary duplication) and gaps (aspects of businesses or institutions that may fall through the regulatory net) (Klomp & de Haan, 2011).

1.2 Statement of the Problem

Many regulatory elements can be geared towards these economies reaching their development goals without compromising standards of prudent regulation and the sustainability of the financial sector. Mwega (2014) further note that economics lack unanimous consent about how important finance is to an economic development. However, the 2008 financial crisis showed that a stable financial structure is required, because it will have a positive effect on equity and growth. Typically, regulations would be expected to improve effectiveness and reduce any risk of a financial crisis.

Some critics argue that regulation conflict with efficient markets while those promoting regulation such as Sinha *et al.*, (2011), have claimed that if regulation are well structured and controlled then they will make markets more competitive and fair in terms of their performance. In a survey done by Mckinsey and Company, Chiarella et al. (2011) found that new legislation on corporate banking companies in Europe had resulted in substantial credit cost reductions and income remaining far below the levels of 2007. Mwega (2014) conducted a study on financial industry in Kenya. He says Kenya lacks very stringent rules. Financial institutions in Kenya and other developing economies have reported losses on a large scale. Some of these have become insolvent, or have had to be taken over or rescued by their governments. Vianney (2013) conducted a study to determine the relationship between regulation and the financial performance of banks in Rwanda. Mwega (2014) conducted a case study in Kenya's finance market to investigate the potential trade between financial market regulation and sustainability in Kenya. Mureithi (2012) conducted a report on the impact on financial performance of Deposit-Taking Microfinance Institutions

(DTMs) in Kenya from financial regulation. Young (2012) conducted an empirical examination of the transnational lobbying of the Basel Committee on Banking Supervision. This study focused exclusively on one organization where the results cannot be generalized for other sectors. However, the reviewed studies expose knowledge gaps as far as literature on developing countries are concerned. Therefore this study narrows the research gap by investigating the duplicity in regulation and performance of the financial sector in Kenya.

1.3 Objectives of the Study

The general objective of the study was to investigate the duplicity in regulation and performance of the financial sector in Kenya.

The specific objectives were;

- i. To review and identify regulation duplication/competition in existing regulatory framework for the financial sector in Kenya
- ii. To describe how regulatory effectiveness has been measured in empirical literature
- iii. To assess whether the current regulation structure has affected the performance of the financial sector in Kenya
- iv. To suggest potential ways of enhancing regulatory effectiveness in Kenya

1.4 Justification and Significance of the Study

The study is beneficial to the government and financial sector stakeholders in Kenya. They may use the study findings to revisit the regulation strategies to identify the dynamics and shortcomings of regulation management and pay closer attention to the adequacy of regulatory preconditions. Additionally, the findings of this study enrich existing knowledge by adding to the pool of information available in regard to the topic under study. Hence, it is of interest to both researchers and academicians who seek to explore and carry out further investigations.

LITERATURE REVIEW

2.1 Theoretical review

Two theories were found to be relevant to the use of duplicity regulation and its effect on financial performance. The theories that were found to best inform the research constructs are Micro prudential regulation and macro prudential regulation.

2.2.1 Micro prudential regulation

Hanson *et al.* (2011) states according to this principle that banks use government-insured investments to fund themselves. That has the benefit of mitigating bank runs. The Concise Encyclopedia of Economics describes a bank run as when investors withdraw their deposits in great numbers due to the threat that a bank will collapse and will therefore be unable to repay their deposits in total and when necessary. This also leaves the tax payer vulnerable and creates a moral hazard issue in that the covered deposits create an atmosphere that allows the management of banks to take tremendous risks because they know that the tax payer will recoup their losses as they occur. The Prompt Corrective Action (PCA) theory is an essential element of the banking

regulations. It allows banks to take necessary corrective steps to re-establish their capital levels when losses arise. Consequently, central banks regulate capital with the intent of safeguarding the deposit insurance scheme and pressuring the banks to internalize their financial loss. This is moral hazard prevention. They do so either by finding fresh stock market money, or by reducing their assets to bear the losses.

The drawback on this theory, according to Hanson *et al.* (2011), is that when a regulator pressures a bank in difficulty to recover its capital ratio, it is not obsessed with whether the bank generates new capital or wants to sell any of its assets. No matter what the bank chooses to do, its likelihood of failure is drastically reduced. This theory insensitivity makes sense if one or a few financial institutions in a market are in financial difficulty, because if such a bank intends, for example, to shrink its resources by reducing on loans, then the other banks can take the slack. The market share is therefore transferred from a small number of financial institutions in distress to stable ones. Nevertheless, if many of them want to concurrently shrink their properties, this will have a detrimental impact on the economy.

Hanson *et al.* (2011) suggest that if financial institutions plan to slash new loans, then companies will consider credit very costly and thus decrease investment and employment. If, on the other hand, many institutions want to sell the same assets as properties, then the values of these assets will drop dramatically as seen in the US during the 2008 global financial crisis, in which the house prices fell sharply as financing became too costly for most mortgage lenders to pay and many people displaced from their homes. The final outcome is credit crunches intensifying further.

2.2.2 Macro prudential regulation

Hanson *et al.* (2011), clarify that this hypothesis is characterized by “an attempt to monitor the social costs associated with excessive balance sheet shrinkage on the part of several financial institutions hit with a common shock”. his theory addresses the problem of the economic and financial strain placed on an economic system when many financial institutions simultaneously shrink their assets, and also why these financial institutions would not recoup the costs by increasing fresh capital instead of reducing their assets, or why they don't make sure they have a large capital base well in advance to enable them to withstand a shock.

Declining assets, as discussed earlier, have two consequences. When financial institutions cut down on borrowing, credit becomes more costly and job opportunities and investment would decrease as a result. Second, if several banks want to sell the same illiquid assets as mortgage-backed securities, their prices could drop sharply, leading to a worse credit crunch. This theory is aimed at countering the balance between these two inclinations according to Hanson *et al.* (2011). This does not depend on deposit insurance being in existence. Macro prudential regulation is presumed to implement to both the insurance covers and non-insured deposit-takers. Regulators must therefore supervise all operations of financial institutions which can cause harm

2.2 Empirical Review

As such, Arun and Turner (2008) point out that banking supervision deficiencies, particularly those resulting from a lack of adequate managerial incentive, coupled with better pressure from international organizations, have led policymakers to slowly withdraw from the financial sector in

developing countries. Similarly, the priorities of a bank's shareholders, namely the optimization of shareholder returns, do not align with those of the government regulations in that the shareholders are risk-takers, therefore the regulators are risk-averse and their primary issue is financial sector stability (Capiro & Levine, 2009).

According to the micro financial supervision, banks finance themselves utilizing state insured reserves which while helping to reduce banking crises, it generates a moral hazard problem because it contributes to banking institutions taking too many risk factors because they know that the government will support any losses they end up making. Micro prudential legislation mandates that banks take immediate measures to recover their capital ratio in the event of losses (Hanson, Kashyap; Stein 2011). Central banks enforce policies regulating money. The macro prudential principle seeks to reduce the financial effect that is felt in the economy as much as possible as many commercial banks want to sell their assets at the same time to cover their losses, particularly when the resources are similar for instance to property investment (Hanson et al., 2011). The outcome would be a considerable reduction in the asset's market price. This was felt in the U.S. during the 2007 and 2008 global financial crisis. Financial institutions will also cut loans which will raise borrowing costs. This theory is generally assumed to apply to all deposit-takers, whether they are insured or not. Thus, regulators are expected to monitor the activities of all financial firms with a view to removing any activities that may cause economic damage.

In Rwanda, Vianney (2013) conducted a study to determine the relationship between regulation and the financial performance of banks. He adopted a descriptive research design which allowed him to analyse the interaction stated above. The sample size was 10 commercial banks. His results were that regulation isn't a significant predictor of commercial banks' financial performance in Rwanda. He asserts that regulatory framework is a key pillar in the functioning of the financial institutions and through extension to financial stability and prosperity. He suggested that the Rwandan government adopt policies that would help banks work in a favorable environment and that this will establish financial stability for the country's financial organizations. According to this report, regulations don't impact financial institutions' financial efficiency.

Barth, Caprio and Levine (2009) conducted a survey, financed by the World Bank, between 1998 and 2000. The goal of the survey was to examine the relationship between financial regulations and supervisory practices and the efficiency and stability of the banks. The aim of the survey was to gather information on supervisory bank regulations and restrictions for more than 107 countries. In the survey they used regression analyzes. Researchers concluded that there is a negative correlation between limiting a bank's activities and its efficiency and stability as opposed to banks being able to diversify freely into other financial transactions.

Mwega (2014) conducted a case study in Kenya's finance market to investigate the potential trade between financial market regulation and sustainability in Kenya. The research focused on the banking industry. The research followed an analytical approach, which included quantitative studies and concentrated analysis of policies. He states that financial aims to propagate economic growth and the main objective of regulations is to maintain financial stability and boost economic growth. This has to be regulated because if a big focus is put on the financial sector's stabilization, it can hinder growth because, on the other hand, if focus is given on growth, it may contribute to a potential financial crisis. This found that financial sector reforms have improved the banking

industry over the last ten years. New products are being delivered to customers, and the quality of service has been significantly enhanced. Profitability and stability have also gone up. Consequently, reforms have contributed to a rise in productivity according to this report. He says Kenya has a somewhat controlled financial system, however.

A study on the importance of capital requirements in banking competition and stability was conducted by Gudmundsson, Kisinguh and Odongo (2013). It was conducted during the period 2000 to 2011. They used both the Lerner index and the Panzar and Rosse H-statistics to measure the level of competition within the banking industry in Kenya. They also used ROE to assess efficiency and stability at the banks. It means that its advantages begin to be understood the moment the banking sector restructuring starts to take place. The study concluded that there is a positive relationship that supports the evidence that control of capital enhances bank efficiency and financial stability.

Mureithi (2012) conducted a report on the impact on financial performance of Deposit-Taking Microfinance Institutions (DTMs) in Kenya from financial regulation. The research methodology used was both a descriptive method of survey and a cross sectional method. In Kenya the target population was 6 DTMs. She reached to the conclusion that the 2008 supportive Deposit Taking Microfinance Regulations prompted to DTMs improving their financial performance. The regulations result in an increase in the worth of the existing debt, total assets, profit and DTM equity of the depositors. Therefore regulations have a positive effect on commercial profitability of banks.

Otieno (2012) conducted a report on the impact corporate governance has on the financial performance of Kenya's commercial banks. The 44 commercial banks that were operating at the time were its target population. For his thesis he employed a cross-sectional and empirical analysis method. He used SPSS and Spearman coefficient of correlation and regression analysis to determine the magnitude of the financial performance relationship and estimation, respectively. He concluded that a positive link exists between corporate governance and a bank's stability and good results. Corporate governance constitutes 22.4 per cent of commercial banks ' financial results in Kenya.

Mutuku (2008) conducted a research on consolidated financial sector regulation in Kenya. One of the most compelling arguments for consolidation is the need for the structure of regulation to mirror the structure of the industry. Unless the regulators are corporations regulating banking, insurance, securities and pensions, then it is impossible for a regulator to develop a picture of the entity's overall risks to a specific sub-sector. On the contrary, a super authority would've been able to comprehend and control risk across subsectors, and develop policies to address the risks facing the whole conglomerate. Fragmented regulatory bodies would normally not be in a position to consolidate an overall risk analysis of a financial conglomerate. Consequently, an integrated or semi- integrated regulatory system in which banking, securities, pension and insurance regulation is coordinated is a preferred model in addressing these challenges.

Hetamsaria (2011) conducted a study in India on the single financial regulator. He argued that single regulator could generate economies of scale as a larger organization allows finer specialization of labour and a more intensive utilization of inputs and unification may permit cost

savings on the basis of shared infrastructure, administration, and support systems. Unification may also permit the acquisition of information technologies, which become cost-effective only beyond a certain scale of operations and can avoid wasteful duplication of research and information-gathering efforts. Clearly a consolidated regulator will only have one set of service departments such as administration, finance and human resources hence reducing on staff and other overhead costs. Central departments such as legal, research, and public awareness can be unified into a single department in the new super regulator leading to significant cost savings. The commonality of knowledge required in regulating markets gives the single regulator the benefit of economies of scale.

Cornett and Tehranian (2009) conducted a study on an overview of commercial banks: performance, regulation, and market value. The study found out that commercial banks perform several valuable services to sectors of the economy. The effect of a disruption in the provision of the various services on firms, households, and the overall economy when something goes wrong in the commercial banking sector makes a case for the need to monitor performance and market value and to impose regulations that in turn affect bank performance and market value. Although regulations may be beneficial to households, firms, and the overall economy, they also impose private costs that can affect the performance and market value of commercial banks.

Naceur and Omran (2011) conducted a study on the effects of bank regulations, competition, and financial reforms on banks' performance on the Middle East and North Africa (MENA) countries. The study covered a period between 1989-2005 and control for a wide array of macroeconomic, financial, and bank characteristics. The empirical results suggest that bank-specific characteristics, in particular bank capitalization and credit risk, have a positive and significant impact on banks' net interest margin, cost efficiency, and profitability. As for the impact macroeconomic and financial development indicators bear on bank performance, we conclude that these variables have no significant impact on net interest margins, except for inflation. However, inflation shocks seem to be passed mainly through the deposit rates and this type of transmission means that banks bear the entire negative cost of inflation. Also, the results suggest that banks lower their operating costs in a well-developed banking sector environment (as confirmed by the negative and statistically significant coefficient of the bank development variable in the cost efficient regression models). Furthermore, the stock market development variable is always positive and significant in all specifications, suggesting that banks operating in a well-developed stock market environment tend to have greater profit opportunities. Regulatory and institutional variables seem to have an impact on bank performance as the results suggest that corruption increases the cost-efficiency and net-interest margins while an improvement of the law and order variable decreases the cost of efficiency without affecting performance.

Creane (2003) conducted a research on financial development in the Middle East and North Africa. The results of the study revealed that countries should adopt appropriate regulation and macroeconomic policies, encourage competition within the financial sector, and develop a strong and transparent institutional and legal framework for financial sector activities. In particular, there is need for prudential regulations and supervision, strong creditor rights, and contract enforcement. Therefore, government decision makers should eliminate financial repression and support

financial development as important elements of their policy package to stimulate and sustain economic growth.

Young (2012) conducted an empirical examination of the transnational lobbying of the Basel Committee on Banking Supervision. The study revealed that effective banking supervisory practices are not static. They evolve over time as lessons have been learned, and business in banking continues to grow and advance. Supervisors are also quick to urge banks to follow "best practice" and supervisors will provably "practice what they study" in trying to continuously shift to the highest level of supervision. Further support this goal, the additional requirements set out in the core principles outline supervisory activities that meet existing standard standards but relate to the robustness of individual supervision frameworks. As supervisory practices progress, it is anticipated that a number of extra criteria will move upon each modification of the fundamental principles in becoming key requirements as perceptions on the baseline standards change. In this context, the use of critical requirements and additional criteria will lead to the continued validity of the core principles over time.

Stern and Cubbin (2005) focused on the regulatory effectiveness and in specific the impact of regulation and regulatory governance arrangements on electricity industry outcomes. The overlaps arising from having several regulators potentially contribute to a situation called regulatory arbitrage. Regulating entities elect to register products in those sub-sectors where the laws are relatively weak or most cost-effective. It makes shopping sites, since items are not easily divided into traditional subsectors. Consequently, a single regulator can apply uniform standards to all subsectors thus eliminating the motivation for arbitration. Unified oversight could also help promote competitive fairness, eliminating a scenario where different regulators could lay down different rules for different players on the same operation.

2.3 Research gaps

Contextual gap is the gap presented as a result in differences in the contextual properties. Stern and Cubbin (2005) focused on the regulatory effectiveness where the study focused on the electricity industry outcomes. This study's focus is exclusively on the financial sector. Hetamsaria (2011) conducted a study in India on the single financial regulator. India have a slightly different governance from

Geographical gap is a knowledge gap that considers, the untapped potential or missing/limited research literature, in the geographical area that has not yet been explored or is under-explored. Naceur and Omran, (2011) conducted a study on the effects of bank regulations, competition, and financial reforms on banks' performance on the Middle East and North Africa (MENA) countries. The study focused in MENA countries thus presenting a geographical gap. This study aims to contribute to the field of research by analyzing and creating an understanding of the link between duplicity in regulation and its effect on the financial performance in Kenya. Creane (2003) conducted a research on financial development in the Middle East and North Africa. This study focused on different continent with different economy state and level from Africa.

Methodological gap is the gap that is presented as a result in limitations in the methods and techniques used in the research (explains the situation as it is, avoids bias, positivism, etc.). Goodhart, Hofmann, and Segoviano, (2004) conducted a study on Bank regulation and

macroeconomic fluctuations in USA. The study used secondary data while the current study uses literature/desktop review thus presenting a methodological gap. Young (2012) conducted an empirical examination of the transnational lobbying of the Basel Committee on Banking Supervision. This study focused exclusively on one organization where the results cannot be generalized for other sectors. Vianney (2013) conducted a study to determine the relationship between regulation and the financial performance of banks. He adopted a descriptive research design which allowed him to analyze the interaction stated above. This study will adopt a desk study.

Conceptual gap arises because of some difference between the user's mental model of the application and how the previous application actually works or had been applied. Cornett and Tehranian (2009) conducted a study on an overview of commercial banks: performance, regulation, and market value. The study looked at only commercial bank thus presenting a conceptual gap. The current study focuses on financial sector as a whole. Mutuku, (2008) conducted a research on consolidated financial sector regulation in Kenya. The study focused on the concept of financial regulation but the study did not focus on the effects on the financial sector. Mureithi (2012) conducted a report on the impact on financial performance of Deposit-Taking Microfinance Institutions (DTMs) in Kenya from financial regulation. The research focused on DTMs exclusively not the finance sector. Otieno (2012) conducted a report on the impact corporate governance has on the financial performance of Kenya's commercial banks. The research focused on corporate governance, and hence the conceptual gap to study the financial regulation.

METHODOLOGY

The study adopted a desktop literature review method (desk study). This involved an in-depth review of studies related to duplicity in regulation and performance of the financial sector. Three sorting stages were implemented on the subject under study in order to determine the viability of the subject for research. This is the first stage that comprised the initial identification of all articles that were based on duplicity in regulation and performance from various data bases. The search was done generally by searching the articles in the Article title, abstract, keywords. A second search involved fully available publications on the subject of duplicity in regulation and performance of the financial sector. The third step involved the selection of fully accessible publications. Reduction of the literature to only fully accessible publications yielded specificity and allowed the researcher to focus on the articles that related to duplicity in regulation and performance of the financial sector which was split into top key words. After an in-depth search into the top key words (duplicity of regulations, regulations structure, regulations effect, financial performance), the researcher arrived at 13 articles that were suitable for analysis. The drawing and interpretation of research findings and sense which is not a quantitative impact evaluation, was important in this context, which implies that qualitative and thematic analysis was most suitable in this study.

CONCLUSION AND POLICY IMPLICATION FOR FURTHER STUDY

4.1 Conclusion

Some studies have reported the positive impact regulations have on financial institutions efficiency. Whereas others have shown this effect to be very negative. As such, in their analysis of about one hundred firms in many regulated industries, including the financial system, Booth et al., (2008) demonstrate that regulation as an additional governance structure will constrain the management's decisions.

Regulation reduces the influence of management decisions on shareholder capital, resulting in regulatory substitution for internal control structures that are less successful in minimizing disputes between agencies. Indeed, the existence of regulatory bodies that may interfere in the leader's discipline restricts the latter's discretion. Financial nationalization was inversely correlated with financial development, and positively associated with bank incompetence measures.

The study concludes that financial institutions in Kenya and other developing economies have reported losses on a large scale due to under regulation and regulator duplicity. Some of these have become insolvent, or have had to be taken over or rescued by their governments. A single market regulator clearly has its own advantages over multiple regulators. But it is more suitable for well-developed and mature market, like the UK. However, it can be argued that Kenya's economy and political arena are not mature enough to handle a single financial market regulator. In this light it can be asserted that even mature economies such as the United States still have multiple regulators.

4.2 Recommendations

The study recommends the adherence to principles of government, including transparency and participation in the regulatory process to ensure that regulation serves the public interest and is informed by the legitimate needs of those interested in and affected by regulation. This includes providing meaningful opportunities (including online) for the public to contribute to the process of preparing draft regulatory proposals and to the quality of the supporting analysis. Governments should ensure that regulations are comprehensible and clear and that parties can easily understand their rights and obligations. New structures do not guarantee better regulation. More appropriate structures may help but, fundamentally, better regulation comes from stronger laws, better-trained staff and better enforcement. Any country that thinks that tinkering with the structure of agencies will, by itself, fix past shortcomings is doomed to relive its past crises.

Financial institutions are advised to comply entirely with the stipulated legislation, and all banks must be supervised by the Central Bank. This will ensure a stable financial system which plays a major role in the economy. If this sector is stable the economy will prosper and the country will escape financial crisis. Instituting strict regulations would also allow the regulator to identify failing banks and provide remedial action before they fail, and depositors lose their money.

4.3 Recommendations for further study

There exists a research gap in duplicity regulation and performance: The field can benefit from further research into the impact of regulation on consolidating outcomes. Research programs in

other sectors need to be researched on the impact of duplicity regulation on performance may help develop new ideas for comparison purposes.

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