Financial Inclusion and Stability of Commercial Banks in Kenya: Synergies and Trade-offs

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ABSTRACT

As a result of the global financial crisis of 2007-2009, policy makers, regulators and financial institutions have put a lot of efforts to reforms aimed at improving financial stability. At the same time there has been global commitment in promoting greater financial inclusion. Consequently, commercial banks have addressed financial inclusion by designing new services and products targeting unbankable customers. There are important trade-offs and synergies between financial inclusion and stability. Poorly implemented financial inclusion policies can impair stability, and also, there may be important synergies brought by broad use of financial services which help financial institutions diversify risk and hence aid stability. Financial stability can enhance financial inclusion through trust build in stable financial systems and hence increase the use of financial services. Excessive emphasis on financial stability can prolong involuntary financial exclusion especially in times of regulatory tightening in an attempt to boost profits and cut off risky segments. It is therefore important for financial institutions to understand the interlinkages in advancing financial inclusion and stability. This study analyzed the effect of financial inclusion on commercial banks stability with a view of establishing the significant relationship between them. Financial inclusion was measured using bank availability, bank accessibility and bank usage while stability was represented by asset quality (NPL ratio). The findings revealed that financial inclusion had a statistically significant effect on the stability of commercial banks in Kenya during the study period between 2007-2015. Increase in bank availability, accessibility and usage, were found to support stability (synergy) due to increased deposit mobilization and access to credit. Therefore, the paper recommends increasing the banking customers, advancing affordable and accessible banking services to disadvantaged groups in different regions in the country. In this regard, reforms in financial sector should aim at increasing financial inclusion through digital finance which is a cost cutting measure and to ensure that bank stability indicators commensurate in the role of deepening financial intermediation and hence forming an all inclusive and stable financial sector over time.

Keywords: Financial Inclusion, Unbankable, Stability, Synergy, Trade-off, Financial Deepening