THE RELATIONSHIP BETWEEN FOREIGN EXCHANGE TRADING AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS LISTED ON THE NAIROBI SECURITY EXCHANGE IN KENYA

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Abstract

Diversification has remained an important strategy for many firms worldwide backed with logical reasons. These reasons include increased profitability, reduction in risk, and financial resources. The general objective of the study was to sought the relationship between investment diversification and financial performance of commercial banks listed on the Nairobi Security Exchange in Kenya. The study focused on foreign exchange trading investment. Prospect theory guided the study. Descriptive research design adopted; target population was 11 commercial banks listed on NSE. Sample size of 10 banks was used. The study collected secondary data through data collection sheet from 2008-2017.Data analyzed through descriptive statistics. ANOVA was used to test hypothesis at 5%. Findings will be significant to the commercial banks managers who will be informed the extent to which financial performance can be influenced by foreign exchange trading investment hence guiding decision in resource allocation. The study established positive significant relationship between financial performance and foreign exchange trading. Study recommended central bank to adequately put measures to safeguard the value of the domestic currency to safeguard the assets and liabilities of commercial banks.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Banks financial performance has become a favorite subject for many stakeholders such as customers, investors, government and the public. This has forced key players in the industry to employ diversification strategies to improve its return and to gain competitive edge over the competitors .However, adaptation of investment diversification strategy to manage financial performance of commercial banks has not yielded consensus regarding success of this strategy.

1.2 Investment diversification

Foreign trading exchange globally is nature of business specifically the banking sector, whose financial performance has been impacted by foreign currency movement. Result of the study revealed that large USA banks are exposed to foreign exchange risk and that specific bank performance is related to the value of the dollar relative to market baskets of other currencies. Quarterly changes in the net income of largest USA banks are related to changes in various currency indices. It is important to assess how bank earnings respond to changes in value of foreign currencies relative to the USA dollar (Ling, fayman and Casey, 2014).

Foreign currencies is involved in any international trade, the variability of exchange rate is a possible factor which drives the level of profitability of commercial banks in south Sudan, since it affects their intermediation process. Variation in exchange rate may be a source of risk to many banks. Huge losses in foreign exchange may result to organization failures additionally it will cultivate heavy burden on profitability of organizations. (Manyok, 2016).

In Nigeria, Foreign exchange rate significantly affect banks performance. The evidence from regression revealed that exchange rate exerts an impact on financial institutions in general and the banking industry specifically within the overall economy. It was concluded that there is significant impact of exchange rate risk on bank performance and well managed exchange rate is capable of driving and improving performance of commercial banks within the Nigeria economy (Lambe, 2015).

1.3 Financial performance

In Tanzania banking sector has a great impact on the success of the economy accruing from important role in sustaining financial markets. Financial performance of a bank is significant to shareholders, employees and whole economy. It also offers guarantee to depositors. As a result to this maxim, effort has been made in ascertaining financial position of each bank from time to time and also ensuring banks are efficiently and effectively managed (Zawadi 2013).

Financial performance in Kenya has become a favorite subject for bank stakeholders such as customers, investors, government and the general public. Stable and efficient financial systems represent efficient allocation of resources, which is a basis for financial performance leading to achievement of the ultimate objective (Kassa, 2013).

1.4 Statement of problem

Exchange rate is vital to any economy since it plays significant role in various business processes and transactions, it determines the profitability of traded goods and services, guides resource allocation and investment decisions, dictates domestic price levels among others. Commercial banks on the other hand are directly affected by exchange rates since the daily transactions are encompassed by various exchange rates.

As a financial intermediary, the variation in exchange rate could affect the performance of commercial banks in different ways.Whenever home currency is depreciated, bank recognize accounting gain on their foreign currency denominated asset and loss on foreign currency denominated liability (Getachew, 2015).

Fluctuations in exchange rate may be a source of risk to an organization. Huge loss in foreign exchange may result to organization failures in addition to instigating enormous burden on profitability (Manyok, 2016)

Lambe (2015) found significant relationship between exchange management and performance of financial institutions most specifically banks. Langat and Nyandema (2016) asserted that there exist a strong positive relationship between foreign exchange rates and financial performance, positive relationship between exchange rate and financial performance may reflect how fluctuating and volatile exchange rate may have contributed to the growth of profitability of banks. Manyok (2016) concluded that exchange rate fluctuation had a weak negative association with financial performance. Isse and Nageye (2017) revealed negative significant relationship between foreign exchange trading and financial performance.

Due to conflicting result concerning the association between foreign exchange trading and financial performance in the banking industry. The current study south to find out the significance of foreign exchange trading in the influence of financial performance of commercial banks.

1.5 Overall objective

To establish the relationship between investment diversification and financial performance of commercial banks listed in Nairobi security exchange.

1.5.1 Specific Objective

To establish the relationship between foreign exchange trading and financial performance of commercial banks listed on the Nairobi Security Exchange, Kenya.

1.6 Research Hypothesis

H_{o1}: There is no relationship betweenforeign exchange trading investment and financial performance of commercial banks listed on Nairobi Security Exchange, Kenya.

Significance of the Study

Bank managers will benefit from the findings of the study since they willbe informed to what extend foreign exchange trading will influence financial performance which will form base for investment decision towards the portfolio. This is significant in enabling the commercial banks to allocate the available resources towards various investments in regard to their level of contribution to the company.

1.7 Scope of the study

The study coveredinvestmentdiversificationand financial performance of listed commercial banks in Kenya. The research covered all registered commercial banks in Kenya for the period of 10 years between2008-2017. There are 11 registered commercial banks in Kenya according to Nairobi Security Exchange as at 31December 2018.

CHAPTER TWO

LITERATURE REVIEW

2.1 Theoretical Review

2.1.2 Prospect Theory

Psychologist Daniel Kahneman and Amos Trersky developed prospect theory in 1979 as a psychologically realistic alternative to expected utility theory. The theory enables people to understand how investment choices are made in risk environment. The theory gives description on how investors structure and regard a decision, which involves uncertainty. According to the theory investor look at choices in terms of potential gain or losses in relation to specific reference point, which is often the purchase price (Nyamute, 2016). According to prospect theory, people get much cast down as a result of losses as compared to excitement from an equal amount of gain. Investors tend to underrate probable outcomes compared with certain ones. Equally, investors respond differently to the similar situations depending on the magnitude of losses or gain in which they are present (Kahneman & Perttune, 2004).

The theory is relevant as it provides for a non-biased perspective on the relationship between foreign exchange trading and financial performance variables adopted by this study, by providing information that affects investment in commercial banks. Business environment is surrounded with uncertainty, foreign exchange tradingis volatile venture due to its unpredictable movement of exchange rates of various currencies in which the bank deals with in day to day transaction with expectation of return during exchange activities. Theory stipulates the attachment investors assign to gains and losses, hence bank managers to be weary by setting the maximum and minimum level to hold of various currencies to mitigate the loss that might occur in case of devaluation of any currency equally to avoid losing return in case any currency gain value at any time.

2.2 Empirical Literature

2.2.2 Foreign Exchange trading and financial performance of commercial banks

Ling, Fay and Casey (2014) investigated the impact of foreign currency fluctuations on U.S banks profitability. The study covered the period of 40 years on 22 USA large commercial banks. Study adopted dollar, Euro and Asia currencies to represent three large economic blocks in the world. Regression analysis revealed that large U.S banks are exposed to foreign exchange risk whereby specific banks performances are related to the value of the dollar relative to market baskets of other currencies. Study concluded that rise in value of U.S dollars versus various baskets of foreign currencies will enhance the earnings of U.S.

Lambe (2015) assessed the impact of exchange rate risk on banks performance in Nigeria. Main objectives were to establish the impact of exchange rate, interest rate, inflation and total asset on profit after tax. Secondary data was sourced from central bank of Nigeria for period of 17 years (1997-2013). Collected data was analyzed through ordinary Lead Square of multiple regressions. Study found significant relationship between exchange management and performance of financial institutions most specifically banks.

Offiong, Riman and Akpan (2016) researched on Foreign exchange fluctuations and commercial banks profitability in Nigeria. Specific objectives were to establish the effect of bank size, bank divestment, non- performing loans and capital adequacy on commercial bank profitability. Study adopted pooled cross sectional panel analysis. Data Collected from 12 largest banks in Nigeria was analyzed through a balanced panel methodology. Study found bank size and capital adequacy exerted positive significant effect on commercial banks profitability while non- performing loans and bank divestment exerted a negative effect on commercial banks profitability.

Getachew (2015) researched on the impact of exchange rate on the profitability of commercial banks in Ethiopia. Specific objectives being to evaluate how the variation of exchange rate affects the profitability of Ethiopian banks and to examine whether the impact of exchange rate on the bank profitability emanates from its effect on the bank loan growth. Study employed descriptive research design with descriptive statistics, correlation. Period under study 2004-2014. Data was analyzed using regression analysis. Study found exchange rate had statistically significant negative impact on the profitability of commercial banks, exchange rate has statistically significant positive impact on the loan growth of banks and loan growth rate and GDP growth had statistically significant positive impact on banks profitability. Study concluded loan growth, loan loss expense, exchange rate and GPD significantly affect the profitability of Ethiopian commercial banks.

Manyok (2016) did study on effect of exchange rate fluctuation on financial performance of commercial banks in South Sudan. Study objective were to assess the effect of inflation rate, interest rate spread, bank size and exchange rate on return on asset. Study used secondary data from all financial institutions operating in south Sudan. Multiple regression models were adopted to analyze that collected data. Study found exchange rate fluctuation had a weak negative association with financial performance. Study concluded that the interest rates spread has been increasing in the recent years since borrowing had become expensive thus profitable whereas deposit rates were very small.

Isse and Nageye (2017) examined the effect of foreign exchange rate on financial performance of SME in Mogadishu, Somalia. Specifically the study determined the effect of: balance of payment, foreign direct investment, degree of inflation and taxation on financial performance of SME. Through closed ended questionnaire, the study collected primary data from sample of 42 respondents that was selected from population of 142 employees from merchandising company in Mogadishu. Regression analysis revealed negative significant relationship.

Mbubi (2013) researched on effect of foreign exchange rates on the financial performance of firms listed on NSE. Research objectives were to establish the effect of foreign exchange of the imports on the net income of the company, to establish the effect of foreign exchange export sales on net income of the company and to ascertain the hedging policy available in the organization. Research employed descriptive research design for the period 2002 to 2012 on sample size of forty six firms(financial and investment). Questionnaires were used for data collection, data analyzed through regression method. Result found that unrealized foreign exchange gains/loss had an effect on the Net Income of multinational companies. Thus the study concluded that listed firms financial performance is affected by foreign exchange rates movements.

Majok (2015) assessed the effect of exchange rate fluctuations on financial performance of commercial banks in Kenya. Study specific objective were effect of foreign exchange rate, interest rate spread, inflation and size of the bank on financial performance of commercial banks. Multiple regression analysis was used to measure profitability by ROA. Descriptive research design was adopted for period of 2002 to 2014.Seconadry data was collected from sample of forty-three commercial banks in Kenya. Multiple regression analysis was conducted on the collected data. Findings of the study were Foreign exchange and bank size had weak negative effect while interest rate spread and inflation had negative effect on the performance of commercial banks. Study concluded weak negative relationship between exchange rate fluctuation and bank's financial performance.

Mugambi (2016) examined the relationship between foreign exchange trading and financial performance of commercial banks listed on NSE. Study objectives were to establish the foreign exchange rate exposure by commercial banks in Kenya, to determine the relationship between foreign trading and financial performance of listed commercial banks in Kenya and to evaluate the strategic options to manage the effect of foreign exchange risk exposure. Study employed descriptive research design on eleven listed commercial banks for the period 2010 to 2015 with sample size of 44 employees. Secondary data was collected from annual financial statements while primary data through questionnaires and interviews. Analysis was carried out using Statistical Package for Social Science. Findings of the study were that majority of the respondents believe that commercial banks in Kenya are exposed to transaction risk, there exist a significant relationship between trading and financial performance of banks and that commercial banks employ hedging as a strategy to manage foreign risk exposure. Study concluded a significant relationship between forex trading and financial performance.

Langat & Nyandema (2016) conducted study on the influence of foreign exchange rate on financial performance of commercial banks listed in Nairobi Securities Exchange. Objective of the study were to establish the effect of exchange rate fluctuation, interest rate and inflation rate on financial performance of commercial banks listed on Nairobi Security Exchange. The study used a time series correlation research design with sample size of eleven commercial banks that were listed in the Nairobi Securities Exchange between 2006 and 2013.Multivariate linear regression was used to analyze collected data. Findings of the study found exchange rate and interest rate had positive relationship with ROCE and ROA while inflation had negative relationship with ROCE and ROA.

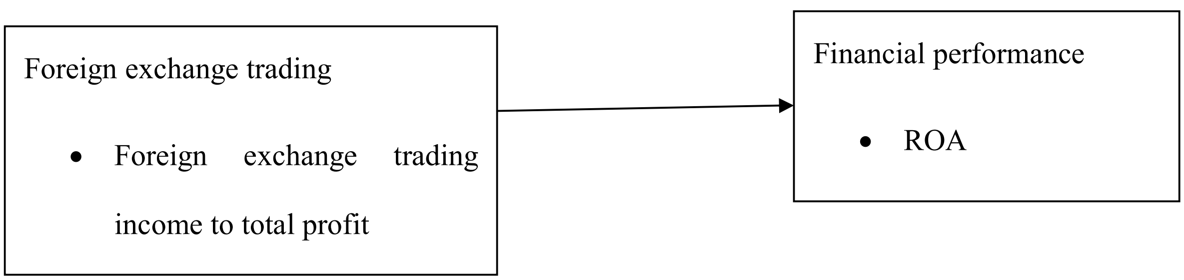
The study concluded that there exist a strong positive relationship between foreign exchange rates and financial performance indicators, positive relationship between exchange rate and financial performance may reflect how fluctuating and volatile exchange rate may have contributed to the growth of profitability of banks.

2.4 Conceptual Framework

Is theoretical structure of assumptions, principles and rules that holds together the ideas comprising a broad concept. The focus of the study was investment diversification and financial performance of commercial banks listed on Nairobi security exchange. In the current study the conceptual framework founded independent variables that directly influencing the dependent variable. The independent variable being foreign exchange trading while financial performance forms dependent variable.

Independent variables **Dependent variable**

Investment diversification strategies



Speculation is the backbone of foreign exchange business, a major motivation behind speculation is the belief that it is profitable. The source of money in foreign exchange trading include sending money to foreign accounts, exchange of currency and transfer of money to foreign accounts where either service fee is changed or interest on top of the currency rate is changed. Commission generated from transactions forms key driver to financial performance of banks.

CHAPTER THREE

RESEARCH METHODOLOGY

3.2 Research Design

A preliminary sketch plan of how a research will take place. The design typically included the instruments that were used, how data was collected, how data was obtained, the way instruments were applied and the predetermined means for analyzing data that was collected. Descriptive research design was employed in the study. The approach was deemed appropriate since the design provides complete profile of the objective under investigation as observed under natural and unchanged environment

3.4 Target Population

Defined as the whole set of items for which the research information is to be used to make conclusion. Thus the target population can be explained as the units for which the results from the research are meant to draw conclusion. As at December 2018, only eleven commercial banks were listed on NSE (NSE, 2018) and this is what formed target population of the current study.

3.5 Sample and sampling design

Sample is a proportion of the population being examined through a research study. The design refers to the define procedure that the researcher will use in selecting the items from the population that will form the sample. While using sampling techniques the researcher has to ensure that the characteristics of the population are accurately reproduced in the sample. The study adopted purposive sample design to establish the sample that represented the entire population. Purposive sampling involves the deliberate selection of particular units of the sample.

3.5.1 Sample size

The sample should be as representative as possible of the entire population. The larger the population the more reliable since it has smaller error while the smaller the population the larger the error hence cannot give true picture of the whole population. The study selected 10 commercial banks listed in Nairobi security exchange to form the sample. National bank of Kenya was excluded because of its long time profits warning which eventually saw it delisted.

3.6.2 Data Collection Procedures

The study utilized secondary data, which was sourced from ten banks published financial statements, CBK supervisory data bank and respective commercial banks annual statements from the year 2008 to the year 2017. Data collection sheet was used to collected data.

3.7 Data Analysis

3.7.1 Descriptive statistics

Analysis of the collected data was conducted through correlation analysis, simple regression analysis and descriptive statistics, which are percentages and mean score for each variable was calculated and tabulated. Results of the study were presented in tables, charts and graphs. Correlation analysis was used to establish relationship between the variables under study, the direction and magnitude of the relationship was determined too. A t-test at 5% level of significance was carried out to determine the significance of independent variable in influencing the dependent variable.

3.7.2 Inferential statistics

Simple regression analysis was carried out to find out the association between predictor variable (foreign exchange trading) and dependent variable (financial performance). In the study thesimple regression model dependent variable (Y) for financial performance and independent variable X1investment being foreign exchange trading.

Simple regression models that was adopted in testing the relationship between foreign exchange trading and financial performance was given by the following equations.

$Y = \alpha + \beta_1 X_{1+} e$ …………………..…………………..…….. Equation

Where:

Y Financial performance

α is constant performance

$\beta_{1,}$ are regression coefficients of the variable

X_1-Foreign exchange trading

Ɛis error margin that may arise from other factors that influence financial performance

CHAPTER FOUR

DATA ANALYSIS AND DISCUSSIONS OF FINDINGS

Descriptive statistics

Foreign exchange trading means any facility offered, business undertaken or transaction executed with any person involving a foreign currency. The foreign exchange trading data from the 10 banks were extracted from the published report. This was measured using foreign exchange trading data on interest income, which was converted into the ratio of foreign trading income (ratio %) on total profit. This variable was important in the determination of the effect of the foreign trading income on the overall financial performance of the financial banks listed in the NSE. The findings are presented in Figure 4.1

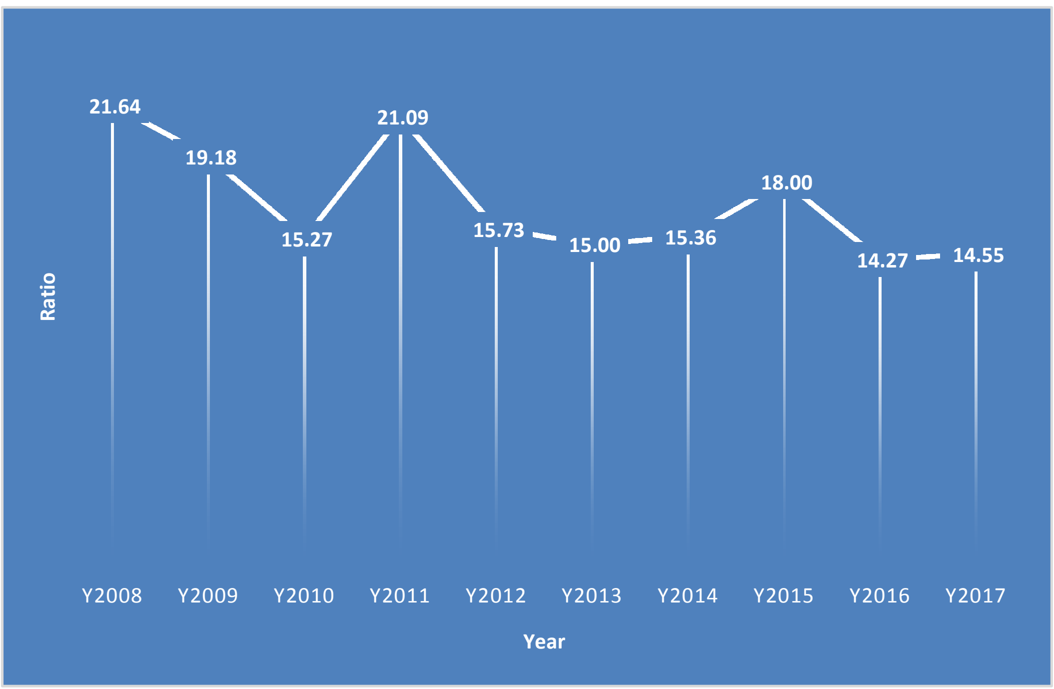


Figure 4.2 Foreign exchange Trading

The findings in Figure 4.1 showed that, in the year 2008 the foreign exchange trading ratio reached 21.64, in 2009 came down to 19.18, in 2010 come down further to 15.27 before rising to 21.09 in 2011. Years 2012 had a drop to 15.73, which further dropped to 15.0 in 2013 and 15.36 in 2014. However, 2015 there was 3-point growth to 18.00, before sharp drop in 2016 and 2017 at 14.27 and 14.55 respectively. Generally, there was a gradual decline in foreign trading income ratio from the year 2008 to year 2010 and then spiking up in 2011 to 21.09 before stabilizing at 15 upto2015 when it rose to 18. Overall, there was erratic behavior over the 10 years period. The fluctuating movement was due to instability of Kenyan currency against the major world currency. The year 2008, Kenya shillings weaken against the US dollar. The increase in demand for US dollar, which was driven by expectation of increased importation of maize, caused the Kenya shilling to depreciate. The study recorded sharp drop in foreign exchange trading ratio in 2010 attributed by Kenyan shillings depreciated throughout the year against all major world and regional currencies. An exchange rate in 2009 was ksh.75 US dollar while year 2010 was ksks.80 US dollar. The weaken against the major currencies in 2010 was associated to increased demand for imports to support improved economic growth.

4.4.6 Financial Performance

Financial performance was important since it determines the ability to leverage operational and investment decision and strategies to achieve a business financial stability. This was dependent variable and was measured using the ROA. The findings were presented in Figure 4.6

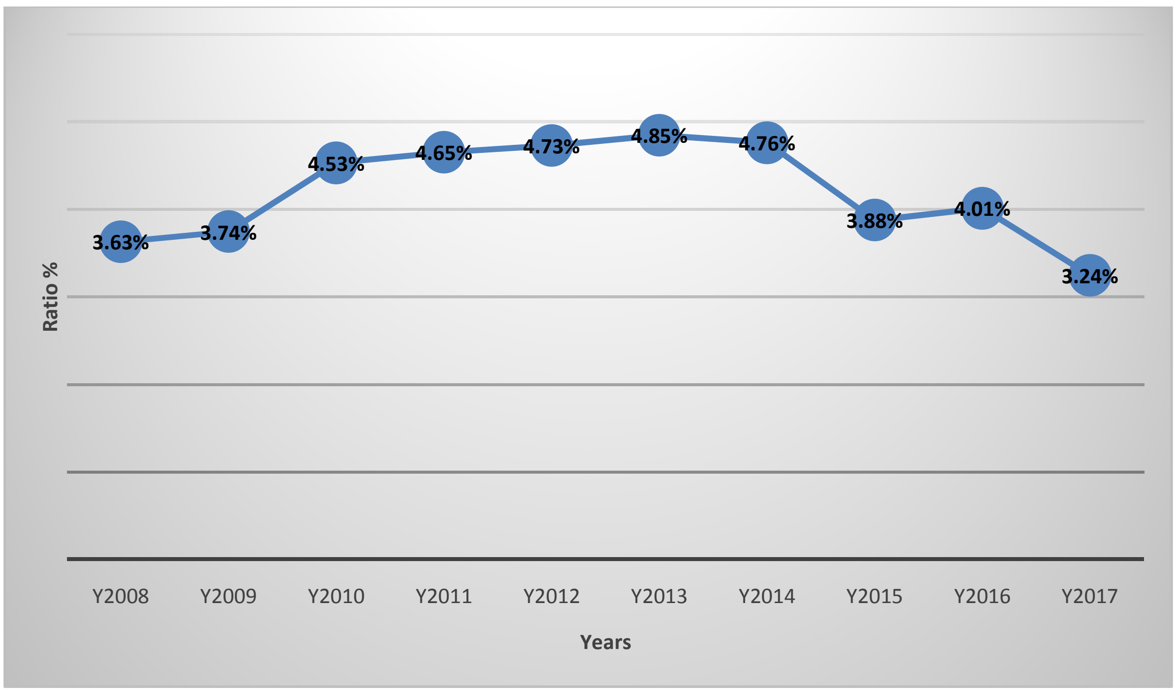


Figure 4.3 Financial performance

The findings shows thatbanksaverage return on asset ranged from 3.24% in the year 2017 being the lowest to 4.85% in 2012, which was the highest over the 10 years period.

Overall, the lowest financial performance was 3.24% in the years 2017 and the highest was 4.85% in the years 2013.Poor performance in 2017 was occasioned by low interest income on loans and advances, which is major source of income for commercial banks. The banking

This was dependent variable of the study, which was measured using ROA. The data for the indicators was presented on graph.2017 had poor performance as exhibited by low ratio which was occasioned by low interest income on loans and advances after CBK introduced capping interest rate, interest income on loans and advance forms major source of income for commercial banks. The decline in interest income was associated with low lending due to subdued economic activities and capping of interest rate by CBK. 2011 was good year as backed up with the highest score of 18.70%. The higher profits were attributed to higher interest income on loans and advances associated with higher interest rate charged by commercial banks during that particular year.

4.5 Correlational Analysis

The study applied Pearson product moment correlation coefficient. Correlations estimate the strength of the linear relationship between two variables. The Correlation Coefficients are illustrated in Table 4.4

Table 4.1: Correlations Coefficient analysis

		Foreign Exchange Trading	Financial Performance2
Foreign Exchange Trading	Pearson Correlation	1	
	Sig. (2-tailed)		
	N	100	
Financial Performance	Pearson Correlation	**.218***	1
	Sig. (2-tailed)	**.022**	
	N	100	100

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

The Pearson correlation coefficient for financial performance and foreign exchange trading was.218(r=218). It implied weak positive correlation. The p-value for this correlation coefficient was 0.022 at 5% level, a significant linearrelationship was illustrated between the two variables since $p<0.05$.

4.7 Simple Regression Analysis

Regression analysis was used to determine the significance of the relationship between the dependent variable and independent variable. This analysis was used to answer the questions; how do the independent variable influence the dependent variable and to what extent does independent variable the dependent variable.

The overall objective of the study was to establish the effect of foreign exchange trading and financial performance of Commercial banks listed on Nairobi Security Exchange, Kenya. To achieve this objective, a specific objective and corresponding hypothes was set and formulated respectively. Simple regression analysis were used to establish the influence of predictor variables on the dependent variable.

4.7.2 Foreign Exchange Trading and Financial Performance

The objective of the study sought to determine the relationship between foreign exchange trading and financial performance of commercial banks listed at the NSE, Kenya. The following equation was used;

$Y = \alpha + \beta_1 (X_1)$

Where α is constant, β_1 is the regression coefficient of foreign exchange trading,

The study set out to determine the independent relationship between foreign exchange trading and financial performance. A regression test was run between foreign exchange trading and financial performance. This section presents the tables and their interpretations.

Table 4.2: Foreign Exchange trading and Financial Performance

Table 4.10a :Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.218[a]	.047	.039	3.115

a. Predictors: (Constant), Foreign Exchange Trading

Table 4.10b: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	52.199	1	52.199	5.380	.022[b]
	Residual	1047.801	98	9.702		
	Total	1100.000	99			

a. Dependent Variable: FinancialPerformance2

b.Predictors: (Constant), Foreign Exchange Trading

Table 4.10 c: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	7.155	.580		12.344	.000
	Foreign Exchange Trading	.068	.029	.218	2.320	.022

a. Dependent Variable: FinancialPerformance2

Source: Research Data, 2020

The results of the analysis in Table 4.2 showed that 4.7% (R^2 =.047) variation on financial performance was explained by foreign exchange trading. The rest 95.3% was explained by other factors outside the model. F value =5.380 with p-value =0.022 p<0.005, Implying that the overall model was significant in predicting the financial performance of commercial banks listed in Nairobi security exchange. Since the study confirmed that there was positive and significant relationship between foreign exchange trading and financial performance. The table 4.2 above indicated that there is positive beta co-efficient of 0.068 as indicated by the matrix coefficient with t=2.320, p-value=0.022<0.05 and a constant of 7.155 with t=12.344, p-value =0.000, p<0.05. Both constant and foreign exchange trading contribute significantly to the model meaning that it is different from zero, hence the model can inform the study of the prediction of the outcome. The regression equation was presented as $Y=7.155X_1$

Where Y is financial performance, X1 foreign exchange trading.

This relationship was expressed in the following equation:

$Y=7.155+ 0.068 X_1$

$Y =0.068 X_1$

In the coefficient table, a unit changes in foreign exchange trading yields .068positive changes on financial performance of commercial banks. This change is statistically significant, meaning that foreign exchange trading impacts financial performance of commercial banks listed in NSE positively. These findings corroborate with earlier study by Langat & Nyandema (2016) whose study concluded that there exist positive relationship between foreign exchange trading and financial performance.

4.8 Hypothesis Testing

H_{o1}: *There is no relationship between foreignexchange trading and financial performance of commercial banks listed on Nairobi Security Exchange, Kenya.*

ANOVA for the linear model presented in table 4.2b of foreign exchange trading and financial performance had F values =5.380 which was significant with p= 0.022<0.05 meaning the model was significant in the prediction of financial performance of commercial banks.Based on the results the study rejected the null hypothesis (H_{o1}).

CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1 Summary of the findings

The study was carried out with the presumption that that foreign exchange trading do not influence financial performance of commercial banks listed in Nairobi security exchange. Empirical literature and theories on two variables were analyzed. To ascertain the extent to which foreign exchange trading impact financial performance, regression tests was carried out. SPSS was used as the statistical tool for analysis.

5.1.1 Foreign exchange and Financial Performance

The objective of the study sought to establish the relationship between foreign exchange trading and financial performance of commercial banks listed on the Nairobi Security Exchange, Kenya. Income generated from foreign exchange trading was used as an indicator measure. Returns from foreign exchange trading lacked consistency over the period of study due to instability of Kenyan currency against the major world currency as backed by descriptive statistics analysis. Regression result table 4.2a suggested a weak positive correlation between foreign exchange trading and financial performance $r=.218$indicating significant linear relationship. Further result from summary model table suggested that 4.7% (R squared=.047) variation on financial performance was explained by foreign trading exchange.

5.2 Conclusion

5.2 .2 Foreign exchange trading and financial performance

H_{o1}*The hypothesis, which stated that foreign exchange trading had no relationship with financial performance of commercial banks listed on Nairobi securities exchange Kenya.*

Coefficient table 4.2c indicated that for every unit invested in foreign trading exchange yielded 0.068 positive change on financial performance which was significant as illustrated by $t=2.320$ with $p=0.022<0.05$.The ANOVA for linear model was used to test the hypothesis result presented in table 4.2b of foreign trading exchange and financial performance has an F value=5.380, which is significant with $p=0.022<0.05$ meaning that the overall model was significant in the prediction of financial performance of commercial banks in Kenya. The hypothesis (H_{o1}) was rejected based on the results since $P<0.022$, and confirmed that foreign exchange trading had positive and significant influence on performance of commercial banks.

Foreign exchange trading is volatile venture due to currency exchange rate unpredictable movement. Commercial banks should be wary on the level of various currencies held at any given time since investing in foreign exchange trading is speculation activities surrounded by uncertainty; unfavorable change in value of major world currencies will result in reduction of banks asset when converted into Kenyan currencies translating to loss of initial capital invested and anticipated interest income. However commercial banks should undertake the investment since the study attested that the correlation was statistically significant to financial performance of commercial banks and equally is good source of short term income whenever the currency rate is favorable hence cushion the banks against unforeseen loss from other diversification strategies.

5.3 Recommendation of the study

Study recommended relevant authority like central bank to adequately put measures to safeguard the value of the domestic currency which in turn will ensure that banks assets (cash in foreign currency) value is not significantly affected by devaluation of other major world currencies. Additionally CBK to put measures in place to control foreign currency fluctuations since it has great impact on the income generated from foreign exchange trading and overall financial performance.

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