effects of leverage on financial performance of listed non financial firms in Kenya

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THE IMPACT OF LEVERAGE ON FINANCIAL PERFORMANCE OF LISTED NON-FINANCIAL FIRM IN KENYA

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Abstract

Literature available shows that financial performance is known variable on Listed Non financial firms in developed economies. This study sought to establish the effects of Leverage on financial performance of listed non-financial firms in Kenya. The objective of the study was to access the impact of leverage on financial performance of listed non-financial firms in Kenya. The study also adopted supporting Static trade-off theory for the study objective. The study used causal research design and the target population constituted 42 listed non - financial firms at the NSE under different categories. The study used secondary panel data contained in the annual reports and financial statements of listed non-financial companies from the NSE Hand Book 2009-2013. A regression model was used to analyze the objective and the results were presented using descriptive statistics and inferential analysis such as Student t test. The results of statistical tests

show that financial leverage has a negative and significant effect on effect corporate financial performance (ROA).

Key words: Leverage, ROA, NSE Hand Book and Static Trade-off Theory

1.0 INTRODUCTION

The importance of financial decisions cannot be over emphasized since many of the factors that contribute to business failure can be addressed using strategies and financial decisions that drive growth and the achievement of organizational objectives. The finance factor is the main cause of financial distress. Financial decisions result in a given financial structure and suboptimal financing decisions can lead to corporate failure.

To understand how firms in developing countries finance their operations, it is necessary to examine the effects of leverage being one of the components of financial structure decisions. Company financing decisions involve a wide range of policy issues. At the macro level, they have implications for capital market development, interest rate and security price determination, and regulation. At the micro level, such decisions affect short term funding and capital structure, corporate governance and company development.

Financial institutions in Kenyan financial sector have been on record of posting billion of shillings in profit and this trend has been on the rise yet non- financial companies which are listed in Nairobi Stock Exchange have not been performing well and some actually records huge losses. Business success depends heavily on the ability of financial managers to effectively manage the components of working capital.

1.1.1 Global Perspective of Leverage and Performance of Listed Non-Financial Firms

Financing structure is critical to the company's performance. The equity financing ratio and operating performance of non - financial sectors listed companies in China has been found to have a significant positive correlation; no significant linear relationship between the endogenous financing ratio and corporate performance; the debt financing ratio and operating performance is negatively correlated (Yan-ru Hui & Liang, 2014). Allen, Chakrabarti and De (2008) assert that while a large number of firms (e.g., in India and Hybrid Sector firms in China) do not use much bank finance, the reason behind their choice is unclear. Is it because these firms are unable to

secure bank credit (e.g., credit rationing, low credit quality) even though they prefer bank credit to alternative finance, or does this financing pattern reflect an interior optimal choice rather than a corner solution. Alternative finance may actually be the preferred form of finance over bank finance because the effective (as opposed to nominal) cost of alternative finance (average over a long period of time) may be lower due to some of its special beneficial features, such as renegotiation flexibility and the advantage of an extended network with the providers of capital. Due to long dated economic policies, the cost of capital is much higher than in more developed countries and many firms suffer from credit constraints (Terra, 2003). Also, the debt market in Brazil is less mature when contrasted to US or European markets, with less transactions and lower liquidity (Sheng & Saito, 2008). Because emerging economies tend to have higher interest rates when compared to more developed economies (Neumeyer & Perri, 2005), the opportunity cost of holding cash is higher.

The balance sheets of non-financial firms in the US were significantly affected during the crisis of 2007. During this period, the decline in the value of assets eroded borrowers' net worth faster than their gross worth (due to their leverage), which led to a reduction in the value of the collateral and subsequent fall in the amounts able to be borrowed (Brunnermeier, 2009). In Egypt, Ebaid (2009) asserted that capital structure in Egypt has little to no impact on a firm's performance while there existed a negative relation between debt ratio and firm performance in Nigeria (Muritala, 2012). In Ghana, the components of financial structure are positively and significantly related with firm value but use of long term debt maximizes firm value more than the equity (Antwi, Mills & Zhao, 2012). In Pakistan, financial leverage has a significant negative relationship with firm performance (Khalique, Abdul, Hassan and Alkali 2012). Also, a negative relationship between capital structure and performance of non-financial firms in Pakistan indicates that agency issues may lead the firms to use higher than appropriate levels of debt in their capital structure. This over leveraging may increase the lenders' influence which in turn limits the managers' ability to manage the operations effectively, hence negatively affecting the firm performance (Nadeem & Wang, 2013). In the US, the near-collapse of Bear Stearns and failure of Lehman Brothers are both characterised as liquidity shocks that had a greater impact on financially fragile non-financial firms. The presented findings show that the improvement in demand expectations positively affected the performances of U.S. non-financial firms in the early months of recovery (Chatelain, 2013).

1.1.2 Financial Performance of Listed Non-Financial Firms in Kenya

Statistics from Capital market Authority (2014) show that Kenyan economy went through a strong phase of economic growth over the period 2003-2007, as the rate of economic growth accelerated up to 7 per cent. During the same period TFP in manufacturing increased by as much as 20% (World Bank, 2007). Aggregate capital formation increased up to 19.5 per cent, which is high by Kenyan standards, but of course pales in comparison with those of its Asian competitors. And it is a long way away from the long-term target of investments of 30% of GDP.

 (Maina and Kondongo, 2013) in Kenya investigated the effect of debt-equity ratio performance of firms listed at the Nairobi Securities exchange and found a significant negative relationship between capital structure and all measures of performance. Otieno (2013) explored the financial structure of listed financial firms in Kenya based on a sample of 29 non financial firms listed on the Nairobi Securities Exchange during the period 2004-2012 and revealed that firm specific factors affecting the capital structure of listed firms in Kenya are asset tangibility, firm's profitability, size of the firm, firm's growth opportunities and finally liquidity of a firm's assets while the macroeconomic factors are economic growth and corporate tax rate.

1.2 Statement of the Problem

Business success depends heavily on the ability of financial managers to effectively manage the financial structure components (Filbeck & Krueger, 2005). Studies from developed countries show that non financial firms are experiencing declining performance and data shows that non financial firms have been delisted from the Stock exchange in the last decade (Tian & Zeitun, 2007). Documented evidence available from the World Bank (2014) shows that non financial firms in Kenya are characterized by a decline in financial performance for example, Kenya Airways made a loss of Sh3.4 billion after tax by March 2014, down from Sh7.8 billion it made in 2013 (Wahito, 2014). Further statistics from the Capital market Authority reveals that market price of the shares declined in the year 2007 – 2013 (CMA, 2013). More evidence available in Kenya for example Furniture firm Hutchings Biemer which was listed on the commercial and services sector, had been suspended for over ten years before being de-listed from the Nairobi Stock Exchange in 2006 (Wandera, 2006). Reports from the Republic of Kenya (RoK) reveal that the low financial performance is a major hindrance in the realization of Vision 2030 leading

to a lower economic development and loss of jobs in Kenya which is associated with social injustices (RoK, 2014).

Information available from the foregoing background reveals that momentous efforts to revive the ailing and liquidating companies have focused on financial restructuring. However managers and practitioners still lack adequate guidance for attaining optimal financing decisions (Kibet, Tenei & Mutwol, 2011) yet many of the problems experienced by the companies put under statutory management were largely attributed to financing (Chebii, Kipchumba & Wasike, 2011). This situation has led to loss of investors' wealth and confidence in the stock market. Studies on the relationship between various financing decisions and financial performance have produced mixed results hence determination of optimal capital structure is a difficult task that go beyond many theories though many researchers agree that the economic and institutional environment in which the firms operate significantly affect the capital structure of a firm (Owolabi & Inyang, 2013). Appropriate financing/capital structure should be profitable to the firm to enable it meet its obligations. It is against this background that this study was carried out.

1.3 Research Objective

The main objective of the study was to assess the Impact of leverage on financial performance of listed non-financial firms in Kenya.

1.3.1 Specific Objective

The specific objective was:

To establish the extent which leverage affected financial performance of listed non-financial firms in Kenya.

1.4 Research Hypotheses

The research hypothesis was;

H_0: Leverage does not affect financial performance of listed non-financial firms in Kenya

2.2.1 Static Trade-off Theory

The static trade-off theory of capital structure states that optimal capital structure is obtained where the net tax advantage of debt financing balances leverage related costs such as bankruptcy. Trade-off theory actually supports the leverage to construct capital structure by assuming leverage-benefits. The tradeoff theory assumes that there are benefits to leverage within a capital structure up until the optimal capital structure is reached. The theory recognizes the tax benefit from interest payments. Studies suggest, however, that most companies have less leverage than this theory would suggest is optimal (Modigliani & Miller, 1958). Optimal level of leverage is achieved by balancing the benefits from interest payments and costs of issuing debt. Financially, debt is considered beneficial because of the debt-tax-shields that help to minimize expected tax bills and maximize the after-tax cash flows (Modigliani & Miller, 1958). Trade-off theory hence predicts the cost and benefit analysis of debt financing to achieve optimal capital structure. There is evidence in favor of the static tradeoff and optimal financing structure. Several authors, such as (Schwartz and Aronson 1967), have documented evidence of strong industry effects in debt ratios, which they interpret as evidence of optimal ratios. (Long and Malitz 1985) show that leverage ratios are negatively related to research and development expenditures, which they use as a proxy for intangible assets. (Smith and Watts 1992) also document a negative relation between growth opportunities and debt ratios. (Mackie-Mason 1990) reports evidence that firms with tax loss carry forwards are less likely to issue debt. This conclusion is consistent with Miller and Modigliani (1966), who detected the positive effects of interest tax shields in the market values of electric utilities.

Previous research on static trade-off theory concludes mixed results. On one side, study shows that target leverage is not important. Many studies for instance, (Titman and Wessels 1988), (Rajan & Zingales1995) and (Fama & French, 2002) affirm that higher profitability firms tend to borrow less, which is inconsistent with the actual trade-off prediction that higher profitability firms should borrow more to reduce tax liabilities. (Graham, 2000) estimating the cost and benefit of debt, finds that the large and more profitable firms with low financial distress expectation use the debt conservatively. Microsoft is the classic example of those studies that it being a very profitable organization has maintained a zero-debt policy. Further survey of corporate executives shows the softness of target leverage (Graham & Harvey, 2001). Speed of

adjustment towards target leverage is slow (Jalilvand & Harris, 1984); (Fama & .French 2002). Firms on their capital structures do not compensate the impacts of stock returns actively and prior stock returns are the main determinant of market leverage (Welch, 2004). On the other side, many studies support trade-off theory and confirm the role of target leverage (See e.g. Marsh, 1982; Hovakimian, Opler & Titman, 2001; Korajczyk & Levy, 2003; Hovakimian, 2004; Hovakimian & Tehranian, 2004). (Frank & Goyal 2004) favor the trade-off theory in leverage decisions by examining relative importance of 39 factors. (Flannery & Rangan, 2006) contradict Welch (2004) by finding the effects of firms" prior stock price movements. Most of the time firms are not so active with respect to their financial policy but to move towards target leverage firms do buy back their securities (Leary & Roberts, 2005; Hovakimian, 2006). (Strebulaev 2004) and (Hennessy & Whited 2004) have tried to conciliate inconsistent empirical findings with respect to trade-off theory in a dynamic framework. This theory instigates the null research hypothesis: Leverage affects the financial performance of listed non-financial firms in Kenya

2.3 Conceptual Framework

In a broad sense a conceptual framework can be seen as an attempt to define the nature of research (Gay, 1992). This study sought to access the impact of leverage on financial performance of firm in Kenya. The independent variable in this study was leverage. This study will therefore establish the impact of the independent variable on the dependent variable which is financial performance of listed non-financial firms.

Independent Variable   **Dependent Variable**

| **Leverage** |
| • Debt/Equity |

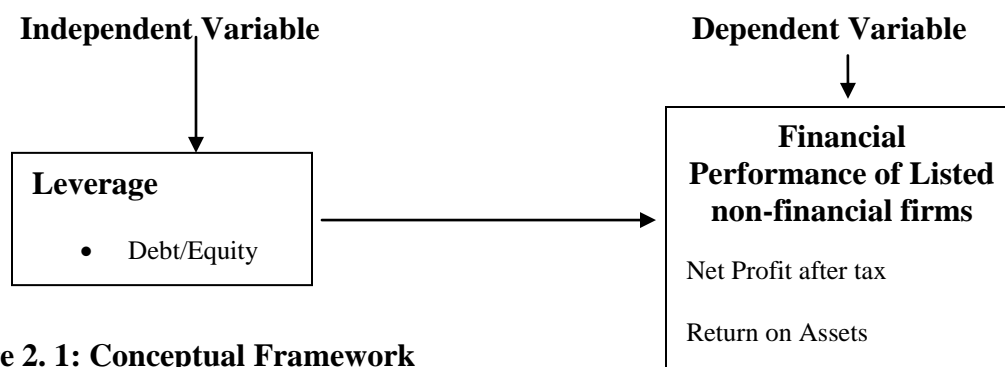| **Financial Performance of Listed non-financial firms** |
| Net Profit after tax |
| Return on Assets |

Figure 2. 1: Conceptual Framework

2.4 Leverage

The financing or leverage decision is a significant managerial decision because it influences the shareholder's return and risk and the market value of the firm. The ratio of debt-equity has

implications for the shareholders' dividends and risk, this affect the cost of capital and the market value of the firm (Tikkiwal & Pandey, 2007). (Gupta and Zeithaml 2006) cited some studies showing contradictory results about the relationship between increased uses of debt in capital structure and financial performance. (Berger and Bonaccorsi di Patti 2006) examined capital structure and firm performance which was a new approach to testing agency theory and an application to the bank industry. Berger and Bonaccorsi di Patti (2006) were the first to employ a simultaneous-equations model that accounts for reverse causality from performance to capital structure. We also control for measures of ownership structure in the tests. The study employed a number of different measures of firm performance which include: financial ratios from balance sheet and income statements; stock market returns and their volatility; and Tobin's Q, which mixes market values with accounting values. The study reported a positive relationship between leverage and financial performance, while (Gleason et al, 2000), (Simerly and Li, 2000) showed negative relationship between financial performance and leverage level. (Zeitun and Tian 2007) found a significantly negative relationship between financial structure and corporate performance. In other words, firms can take advantage of debt to make a better return on equity. (Nazir and Afza, 2008) and Chiou, Cheng and Wu 2006) measured leverage by the debt ratio leverage calculated by the total liabilities divided by total assets. Apphumani (2008) measured leverage as total long-term debt capital divided by equity. In this study, debt level (DEBT) will be measured as long term debt divided by total assets.

2.5 Test of Hypotheses

Hypothesis 1

H_0: Leverage does not affect financial performance of listed non-financial firms in Kenya. To test the hypothesis, the following regression model was used:

Model II: $Y = c + \beta_2 Lev + \varepsilon$

Where: c is the constant,

β_2 shows the change in the dependent variable for a unit change in leverage (Lev) and

ε is the error term.

Table 3. 1 Operationalisation and Measurement of Study Variables

Variable	Name of Variable	Operationalisation	Measurement	Hypothesis Testing
		Total assets	Debt ratio leverage	Student t-test and
		Total liabilities	calculated by the total	2-tail test
Independent	Leverage	Amount of debt	liabilities divided by total	
		borrowed	assets	

RESULTS AND DISCUSSION

4.1.1 Financial Performance of Listed Non-Financial Firms in Kenya

Statistics from Capital Market Authority (2014) Kenyan economy went through a strong phase of economic growth over the period 2003-2007, as the rate of economic growth accelerated up to 7 per cent. During the same period TFP in manufacturing increased by as much as 20% (World Bank, 2007). Aggregate capital formation increased up to 19.5 per cent, which is high by Kenyan standards, but of course pales in comparison with those of its Asian competitors. And it is a long way away from the long-term target of investments of 30% of GDP.

Maina and Kondongo (2013) investigated the effect of debt-equity ratio performance of firms listed at the Nairobi Securities exchange and found a significant negative relationship between capital structure and all measures of performance.

4.3 Descriptive Statistics

4.3.1 Leverage

Leverage had the mean value of financial leverage is 2.2995. This shows that, on average, non-financial companies used for the study were highly geared. The greatest proportions of their resources were financed by long term debt. The standard deviation of 12.05404 signifies a great variation in financial leverage as evidenced by the fact that the minimum observed financial

leverage was 0 while the maximum was 77.59.According to the Economic Survey (2013) the growth experienced in the banking sector increased credit to the private sector by 30.8 percent in 2011 and 11.8 percent in 2012.The increased access to credit may therefore explain the observed phenomenon on financial leverage

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Table 4.1 Leverage Descriptive Statistics: 2009-2013

Year	2009	2010	2011	2012	2013
Minimum	.00	0.00	0.00	0.00	0.00
Maximum	1	0.88	387.15	.3860	0.78
Mean	.4334	.4148	9.8603	.3860	.4031
Std Deviation	.26025	.22805	60.39662	.22787	.23901
N	42	42	42	42	42

4.4. Regression Analysis

When performing ordinary linear regression with SPSS, in order to conclude with methods for examining the distribution of variables to check for non-normally distributed variables as a first look at checking assumptions in regression. Without verifying that your data have met the regression assumptions, your results may be misleading. We therefore need to test whether data meet the assumptions of linear regression. In particular, we will consider the following assumptions; Linearity - the relationships between the predictors and the outcome variable should be linear; Normality - the errors should be normally distributed - technically normality is

necessary only for the t-tests to be valid, estimation of the coefficients only requires that the errors be identically and independently distributed; Homogeneity of variance (homoscedasticity) - the error variance should be constant; Independence - the errors associated with one observation are not correlated with the errors of any other observation and Model specification - the model should be properly specified (including all relevant variables, and excluding irrelevant variables)

Additionally, there are issues that can arise during the analysis that, while strictly speaking are not assumptions of regression, are none the less, of great concern to regression analysts. These issues are; Influence - individual observations that exert undue influence on the coefficients and Collinearity - predictors that are highly collinear, i.e. linearly related, can cause problems in estimating the regression coefficients.

4.5 Diagnostic Tests

Diagnostic tests was performed to make sure that the model chosen was a good model in the sense that all the estimated coefficients had the right signs and were statistically significant on the basis of the *t* and *F* tests (Gujarati (2003).

4.5.1 Multicollinearity, Tolerance and VIF

Multicollinearity in the regression model was detected by testing the R^2 value and analyzing the correlation matrix (Ghozali, 2002).Tolerance values and VIF were also used to measure multicollinearity (Hair et al., 1998). The tolerance values are a measure of the correlation between the predictor variables and can vary between 0 and 1. The closer to zero the tolerance value is for a variable, the stronger the relationship between this and the other predictor variables (Van Horne, 1998).

From the findings the leverage variable had a tolerance and VIF value of 1 indicating that there exist a strong relationship between the dependent variable (firms performance) and the independent variables (Leverage).

Table 4. 2 Multicollinearity, Tolerance and VIF

Study Variable	Collinearity Statistics	
	Tolerance	VIF
Leverage	1.000	1.000

4.5.2 Serial Correlation Test

Serial correlation was also carried out to test errors associated with a given time period being carried over into future time periods. A popular test for serial correlation the Durbin-Watson statistic was used. Fisher (1935) and Pitman (1937) view the DW as the test of choice because of (i) its high power; and (ii) its limited size distortions.

As from the findings the DW score was as tabulated below. The DW is approximately 2 .The DW statistic always lie in the 0-4 range, with a value near two indicating no first-order serial correlation. Positive serial correlation is associated with DW values below 2 and negative serial correlation with DW values above 2.

Table 4. 3 Serial Correlation Test

Study Variable	Durbin-Watson
Leverage	1.944

4.5.3 Stationarity Test

A test for stationarity was also carried out for all the four independent variables. Stationarity is important for estimation; applying least squares regression on non -stationary variables can give misleading parameter estimates of the relationships between variables. Checking for stationarity

can also be important for forecasting. It can help about what kind of processes will have to be built into the model in order to make accurate predictions. (Dielbold & Killian 1999).

The study used Autocorrelation test to show stationarity of the data used as shown below:

Table 4. 4 Autocorrelations Test

Series: DATA2009 2013

Lag	Autocorrelation	Std. Error[a]	Box-Ljung Statistic		
			Value	Df	Sig.[b]
1	-.014	.147	.009	1	.925
2	.024	.144	.036	2	.982
3	-.071	.147	.270	3	.966
4	-.020	.138	.291	4	.990
5	-.001	.144	.291	5	.998
6	.048	.135	.416	6	.999
7	-.053	.132	.581	7	.999
8	-.048	.138	.700	8	1.000
9	-.088	.125	1.202	9	.999
10	-.007	.132	1.205	10	1.000
11	-.011	.132	1.212	11	1.000
12	-.050	.128	1.362	12	1.000
13	.053	.128	1.534	13	1.000
14	.074	.121	1.906	14	1.000
15	.008	.125	1.910	15	1.000
16	-.066	.125	2.191	16	1.000

a. The underlying process assumed is independence (white noise).

4.5.4 Test for Normality

A test for stationarity was also carried out for all the four independent variables. Stationarity is important for estimation; applying least squares regression on non -stationary variables can give misleading parameter estimates of the relationships between variables. Checking for stationarity can also be important for forcasting.It can help about what kind of processes will have to be built into the model in order to make accurate predictions. Dielbold & Killian (1999)

Table 4.5 Tests of Normality

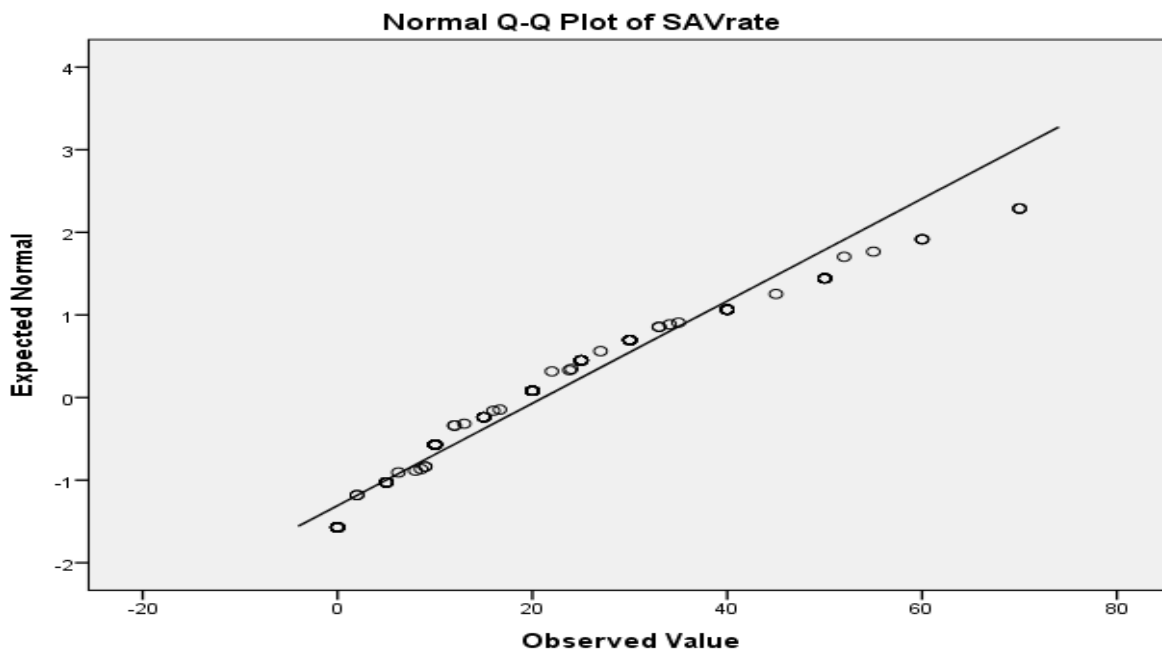|	Kolmogorov-Smirnov[a]			Shapiro-Wilk		
	Statistic	Df	Sig.	Statistic	Df	Sig.
Independent variables	.150	180	.000	.924	180	.000

a. Lilliefors Significance Correction

Figure 4.2

4.6 Regression Analysis: Leverage

The financing or leverage decision is a significant managerial decision because it influences the shareholder's return and risk and the market value of the firm. Leverage or capital structure ratios assure the long-term creditors about a firm's ability to repay the principal amount on maturity and to make periodic payment of interest thereon. Thus, there are two aspects of long term solvency of a firm, viz, ability to repay the principal amount on maturity and regular payment of interest. Accordingly, there are two different types of mutually dependent and inter-related leverage ratios. The first type of leverage ratios, computed from the balance sheet and based on the relationship between capital and owners equity capital ,he second type of leverage ratios, popularly known as coverage ratios, are calculated from the profit and loss account and include many variations such as, interest coverage ratios; dividend coverage ratio and total fixed charges coverage ratio. Have many variations such as, debt-equity ratio, propriety ratio and equity-assets ratio. The ratio of debt-equity has implications for the shareholders' dividends and risk, this affect the cost of capital and the market value of the firm (Tikkiwal & Pandey, 2007).

4.6.1 Model summary

From the findings Leverage variable explain only 0.1% of the performance as represented by the R^2. This therefore means that there are other factors not studied in this research that majorly contributes to the firms' performance.

The value of the Durbin-Watson statistic ranges from 0 to 4. As a general rule of thumb, the two variables are uncorrelated since the Durbin-Watson statistic is approximately 2.A value close to 0 indicates strong positive correlation, while a value of 4 indicates strong negative correlation.

The value of Durbin -Waston is 1.944, approximately equal to 2, indicating no serial correlation

Table 4.6: Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.038[a]	.001	-.024	4.82370

a. Predictors: (Constant), Leverage

b. Dependent Variable: Performance ROA

4.6.2 ANOVA

The F critical at 5% level of significance was 4.0847. Since F calculated is less than the F critical (value =0.057), this shows that the model was insignificant.

Table 4.7: ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	1.333	1	1.333	.057	.812[b]
1	Residual	930.725	40	23.268		
	Total	932.058	41			

a. Dependent Variable: Performance ROA

b. Predictors: (Constant), Leverage

4.6 3 Effects of Leverage on financial performance of listed non financial firms

Model II Y= c + β_2Lev + ε

Where: Lev is the Leverage can be written as

$Y = 1.297-0.003X_1$

Implying that a unit increase in leverage will lead to 1.297- 0.003 decreases in the dependent variable that is ROA. The result indicates that LEV has a negative insignificant association with ROA. This implies that any increase in LEV will significantly decrease ROA, which means that reducing debt level will leads to significant increase in firm's performance.

The tolerance value (VIF) is 1 and since the closer to 1 is a variable, the stronger the relationship between the variable and the other predictor variables therefore leverage has a strong relationship with performance. Gupta and Zeithaml (2006) cited some studies showing contradictory results about the relationship between increased uses of debt in capital structure and financial performance. While Gleason et al (2000), Simerly and Li (2000) showed negative relationship between financial performance and leverage level.

Zeitun and Tian (2007) found a significantly negative relationship between financial structure and corporate performance. In other words, firms can take advantage of debt to make a better return on equity. The study findings are also in line with H.M Alarm in his study "The impact of working capital management on profitability and market valuation of Pakistani firms" whom in his study found a negative association between ROA and leverage. Further the study conquers with Abdul (2012) findings who in his study concluded that financial leverage has a significant negative relationship with the firm performance as measured by return on assets (ROA).

Table 4.8: Effect of Leverage on financial performance

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.297	.758		1.712	.095
	Leverage	-.003	.013	-.038	-.239	.812

4.7.1 Hypotheses Testing

The results of hypotheses testing showed that, Leverage had negative insignificant relationship with financial performance. This means that leverage does affect immensely to financial performance.

H_0 leverage does not affect financial performance of listed non financial firms at significance level of 0.05; the outcome showed that significance level of 0.01 which is less than 0.05 meaning

we reject the null hypothesis and conclude that Leverage has a an effect on financial performance.

5.0 Summary of findings

The mean value of financial leverage is 2.2995. This shows that, on average, non-financial companies used for the study were highly geared. The greatest proportions of their resources were financed by long term debt. The standard deviation of 12.05404 signifies a great variation in financial leverage as evidenced by the fact that the minimum observed financial leverage was 0 while the maximum was 77.59.According to the economic survey (2013) the growth experienced in the banking sector increased credit to the private sector by 30.8 percent in 2011 and 11.8 percent in 2012.The increased access to credit may therefore explain the observed phenomenon on financial leverage.

5.2 Conclusion

The results of statistical tests shows that financial leverage has a negative and insignificant effect on corporate performance (ROA). We therefore reject the Null hypothesis: Leverage does not affect financial performance of listed non-financial firms in Kenya

5.3 Recommendations

The Financial Manager should be careful not to over borrow since leverage would reduce financial performance of the firm. The study recommends that efforts should be made by management to improve the performance of the firms such as to carry out a policy to maximize the use of debt in capital spending activity.

5.4 Areas for further Research

The R^2 was only .40% this means that there other factors that explain the performance of non financial firms. Future research studies should investigate these factors.

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