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THE RELETIONSHIP BETWEEN FINANCIAL LIBERALIZATION AND ECONOMIC GROWTH IN KENYA.

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Abstract

Financial liberalization in Kenya is much more recent. Ceilings on bank lending rates were not removed until July 1991. The central bank continued to announce guidelines for the sectoral composition of bank credit expansion, although these were not strictly enforced after interest rate liberalization. Although the Kenyan authorities have allowed market forces to play a relatively influential role in the financial system, the government maintains a formidable presence in the financial sector. The primary function of the central bank is to regulate the flow of money and credit in order to maintain economic stability, efficiency and growth of the country. To earn profit is the secondary objective of the Central Bank but the main motive is to regulate the monetary and credit system of the country and to foster its growth in the best national interest with a view to securing monetary stability and full utilization of the country's productive resources. These regulations provide guidelines for opening of accounts, limit against advances, setting up of internal audit system, requirement for minimum capital and reserves for a banking company, maintenance of liquidity assets for every banking company, detecting banking frauds etc. The Central Bank of Kenya was established in May 1966. The powers and operations of the Central Bank of Kenya are governed by the Central Bank of Kenya Act 1966, and the Banking Act 1968. The study used descriptive technique and carried out a meta- analysis study. This study exclusively secondary data. The study used Statistical Package for Social Sciences for data analysis (SPSS) to analyze the data and the data findings were presented in tables and figures. The study carried out regression analysis to establish the relationship. The study findings established that in the year 2003, the lending rates were rates were 16.37%. These rates

decreased in the year 2004 to 12.53%. Since then, the lending interest rates increased gradually to 19.65% by the year 2011. In the year 2012, there was a rapid increase in lending interest rates whereby the rates increased to 19.65%. Foreign assets as found by the study had been increasing over the study period with exception of the 2008 financial year. Foreign assets stood at USD. 110,991 million in the year 2003. Foreign assets increased thereafter to stand at USD. 115,774. After the year 2007, foreign investment dropped slightly in the year 2008 to USD 223,549 before picking up a positive trend again from the year 2009 till 2012 were it amounted to USD 374,457.

The study inferences established a positive perfect correlation between the dependent variable, ***Financial Liberalization*** *and the independent/ explanatory variable,* ***Economic growth*** *as evidenced by the empiricism from the operational variables in lieu of the current account, Lending rates and Capital controls.*

Key Words: *Financial Liberalization, Capital Controls, Interest Lending Rates, Current Account & Economic Growth.*

1. Introduction

1.1 General Background

Williamson and Mahar (1998, 2) comprehensively outlines financial liberalization as freeing the market and allowing the forces of demand and supply to determine market prices, grants and credit. Johnston and Sundararajan (1999, 2–3) explores this policy process in a broader systemic perspective. They state that financial sector liberalization "can be viewed as a set of operational reforms and policy measures designed to deregulate and transform the financial system and its structure with the view to achieving a liberalized market-oriented system within an appropriate regulatory framework."

Financial liberalization refers to measures directed at diluting or dismantling regulatory control over the institutional structures, instruments and activities of agents in different segments of the financial sector. These measures can relate to internal or external regulations (Chandrasekhar, 2004).

Financial liberalization also encompasses the following concepts: Trade Liberalization which refers to the removal or reduction, of restrictions or barriers on the free exchange of goods and services between nations. This includes the removal or reduction of both tariff (duties and surcharges) and non-tariff obstacles (like licensing rules, quotas and other requirements). The easing or eradication of these restrictions is often referred to as promoting "free trade." Those against trade liberalization, claim that it can cost jobs and even lives, as cheaper goods flood the market (which at times may not undergo the same quality and safety checks required domestically). Proponents, however, say that trade liberalization ultimately lower consumer costs, increases efficiency and fosters economic growth McCulloch NA *et al* (2001).

Deregulation of Interest Rates that entails a movement towards or an entire privatizing of the interest-rate; making it more free-market dictated rather than by government-regulated means.

Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

Liberalization will likely result in higher interest rates, discourage marginal investment, improve the effectiveness of intermediation and monetary transmission, and enhance the financial access of underserved sectors. This also encourages savings, as the returns on savings are more rewarding hence savers will seek to gain from the improved interest rates. On the downside however, higher interest rates will lead to higher cost of capital and this may lead to inflation/ inflationary environment in a country.

1.1 Financial liberalization

According to Kaminsky and Schmukler (2003). Financial liberalization consists of the deregulation of the foreign sector capital account, the domestic financial sector, and the stock market sector viewed separately from the domestic financial sector. The financial system performs a number of important functions in an economy. Basically, it takes care of mobilizing financial resources, facilitating risk management, allocating resources to the most efficient projects, monitoring the use of financial resources (exerting corporate governance), and providing a payment system that makes trade among economic participants more efficient(Levine, 1997).

Financial development occurs when a financial system is able to improve on performing these functions. There is a large body of theoretical and empirical work emphasizing that financial development is positively associated with economic growth. Closely related to the discussion of the relationship between finance and growth is the discussion of the role that financial liberalization can play in this relationship. The main idea is that financial liberalization may impact on financial development which, in turn, affects economic growth.

1.2 Economic Development

In Sub Saharan Africa, Kenya is the largest economy with an estimated population of 39.8 million. In 2009,

Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

Kenya‟s gross domestic product (GDP) was 29.5 billion with an annual growth rate of 2.6 percent. Although Kenya is currently in a stage of growth, there are still several factors inhibiting economic development and contributing to the poverty trap. According to the 2009 Human Development Report, 20 percent of the Kenyan population lives on less than 1.25 USD a day, and approximately half of the population lives below poverty. (African Economic Outlook, 2010).

Despite Kenya‟s recent crisis, the economy appears to be on track to reverse their poor performance from 2007 to 2008. Kenyan government introduced a strategy called Vision 2030 in 2008 that funded investment growth through increasing credit supply to the private sector, and infrastructure investments to the public sector. This strategy assisted the economy‟s recovery and contributed to a

GDP growth of 2.6 percent in 2008, and is expected to provide a push to accelerate economic growth in subsequent years.

(African Economic Outlook, 2008: 34).

Seers (1979) postulates the purpose of development is to reduce poverty, inequality, and unemployment. For Sen (1999), development involves reducing deprivation or broadening choice. Deprivation represents a multidimensional view of poverty that includes hunger, illiteracy, illness and poor health, powerlessness, voicelessness, insecurity, humiliation, and a lack of access to basic infrastructure (Narayan et al. 2000:4-5).

According to Prof. Meier and Baldwin; "Economic development is a process whereby an economy's real national income increases over a long period of time". Some economists like Profs. Baran, Buchanan and Ellis interpret economic development as something more than merely an increase in total output; they believe that it should also denote a rising

Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

standard of

living. They define economic development as a process whereby the total per capita income or output of a country increases over the long period. Economic development, as it is now generally understood, includes the development of agriculture, industry, trade, transport, means of irrigation, power resources, etc. It, thus, indicates a process of development. The sectoral improvement is the part of the process of development which refers to the economic development. Broadly speaking, economic development has been defined in different ways and as such it is difficult to locate any single definition which may be regarded entirely satisfactory.

1.3 Financial liberalization Economic Development

Financial system in any particular country facilitates the development and growth of the economy. Basically, it takes care of mobilizing financial resources, facilitating risk management, allocating resources to the most efficient projects, monitoring the use of financial resources (exerting corporate governance), and providing a payment system that makes trade among economic participants more efficient(Levine 1997). Financial development occurs when a financial system is able to improve on performing these functions. There is a large body of theoretical and empirical work emphasizing that financial development is positively associated with economic growth. Closely related to the discussion of the relationship between finance and growth is the discussion of the role that financial liberalization can play in this relationship. The main idea is that financial liberalization may impact on financial development which, in turn, affects economic growth.

In the late 1970s and early 1980s, most developing countries were in a crisis of economic policy. Due to adverse circumstances and the deteriorating economic and financial conditions, the

financial system proved to have many deficiencies and was unable to generate economic growth. Based on financial aid from the World Bank and International Monetary Fund, many developing countries in Asia, Europe, Latin America and Africa have undertaken economic reforms to create a suitable investment environment and develop the private sector through an economic system based on market mechanisms. Apparently the result of these reforms was to transform developing economies of many emerging economies, where economic growth is underpinned by strong private sector growth and rapid maturation of capital markets.

1.4 Financial liberalization and Economic Development in Kenya

The interest rate policy in Kenya in the early 1970s was relatively inactive. Thus, compelling the government to regulate interest rates through fixing minimum savings rate for all deposit accepting institutions and minimum lending rates for commercial banks, non-bank financial institutions (NBFIs) and building societies. The official policy in Kenya at that time was to follow a low interest policy in order to encourage investment and protect the small borrowers. This however rendered most interest rates negative in real terms in the 1970s. The first interest rate review was however, undertaken in June 1974 when the minimum savings and lending rates were raised by 2 and 1 per cent respectively (Kariuki, P.W, 1995:5-7).

The financial sector in Kenya is fairly well developed in comparison to most countries in sub-Saharan African countries. The financial sector, measured by the ratio of financial assets to GDP, is relatively deep. The ratio of broad money to GDP, M2/GDP, averaged about 0.30. This compares favorably with other countries in the region where the ratio is abysmally low, ranging from 0.12 in Rwanda, 0.14 in Burundi, to 0.22 in Benin (Abebe, 1990). The diversity of the financial system in Kenya is also manifested in the existence of financial institutions of various types including commercial banks, non-bank

financial institutions, insurance companies, and government monopolized financial parastatals.

Financial liberalization means to give central banks more authority to conduct monetary policy, to privatize and restructure the banking sector, to liberalize interest rates, to waive the direct loans and, more generally, to develop and promote the role of financial markets in financing the economy. The main objective is to enable emerging economies to emerge from recession, and later to develop rapidly. Although the Kenyan authorities have allowed market forces to play a relatively influential role in the financial system, the government maintained a formidable presence in the financial sector. The principal instruments of government's intervention in the financial sector included: (a) ownership of commercial banks, finance companies, the largest pension fund, and an insurance company, which provided the government with extensive direct control over credit allocation;(b) massive public sector financing requirements and borrowing to relend to the parastatal enterprises; and (c) a regime of minimum interest rates on deposits and maximum lending rates (Hanson and Neal, 1986).

2.0 Statement of the problem

Recent theoretical and empirical studies Husain, (2002); Khan, 2003; Iimi, 2004; Trabelsi (2002), also finds economic growth to Granger cause finance in developed countries using a bivariate causality technique. The authors find reverse causality in some countries and bi-directional causality in others. Darrat (1999), while conducting causality tests in Saudi Arabia, Turkey and the UAE, finds growth-led finance evidence in the UAE, finance-led growth in Turkey and a bi-directionality in Saudi Arabia (see Chuah and Thai, 2004). Odhiambo (2004), while conducting a causality test between financial development and economic growth. Husain, 2005; Khan et al., 2005) investigated effects of financial sector reforms. Shan et al (2006) find little support to the hypothesis that financial

Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

development "leads" economic growth. Financial liberalization in Kenya is much more recent. Ceilings on bank lending rates were not removed until July 1991. The central bank continued to announce guidelines for the sectoral composition of bank credit expansion, although these were not strictly enforced after interest rate liberalization. International financial liberalization is even more recent. Offshore borrowing by domestic residents has been permitted only since early 1994, and portfolio capital inflows from abroad were restricted until January 1995. Supporting structural and institutional reforms have yet to be fully implemented. Many banks remain publicly owned and competition among them is limited, Huwpill and Mahmood Prandan (1997).Many studies have been conducted to explore the impact of financial liberalization nexus economic development in emerging economies. According to Kim and Single (2000) they explicitly emphasizes that the liberalisation of controls on financial sector leads to more efficient and effective capital markets in emerging economies, allows the guidance of existing funds and national economies to most productive investments. In contrast, it has also been argued that financial liberalization has led in many cases to disappointing results and in some cases even to economic and financial crises. First, Stiglitz (2000) and others have pointed out that financial liberalization as such does not solve the problem of asymmetric information. This may prevent financial intermediation from becoming more efficient in a liberalized market. This study therefore sought to answer the following question: what is the effect of financial liberalisation on economic growth in Kenya

The Objective of this study was to determine the relationship between

financial liberalization and economic growth in Kenya.

3.0 Research Strategy

The study comprehensively carried out a meta- analysis study. The study effectively explored the descriptive technique. Descriptive research portrays an accurate profile of persons, events, or situations (Saunders, Lewis and Thornhill, 2003). Meta-analysis is a statistical technique to quantitatively synthesise the empirical evidence of a specific field of research. This study sought to investigate and substantiate the impacts of Financial Liberalization to Economic development. Meta-analysis has also become an increasingly accepted research tool in finance and economics phenomena, since it is proving to be very useful for policy evaluations (Pang et al. 1999, Stanley 2001). In this context a Meta-analysis approach was justified as the most effective statistical technique to correlate both the dependent and independent study variables.

This study utilized secondary data from the Central Bank of Kenya (CBK) reports and library in a period of three months. Secondary data has already been collected, analyzed and made available from sources other than yourself (White, 2010). Collecting and analyzing primary data can be expensive and time consuming so where possible the use of secondary data is important. Secondary data from the Central Bank of Kenya (CBK) reports and library were reviewed for completeness and consistency in order to statistical analysis. According to Mugenda (1999), data must be cleaned, coded and properly analyzed in order to obtain a meaningful report. The Secondary data from the Central Bank of Kenya (CBK) reports and library was analyzed using descriptive statistical approach, The excel software was used to transform the variables into a format suitable for analysis after which the Statistical Package for Social Sciences for data analysis (SPSS) which provided various statistics, which then applied to analyze the quantitative data in terms of percentages, frequency distribution, means

and standard deviation. Tables and charts are to be used to summarize responses for further analysis and facilitate comparison. The unity of analysis was essentially secondary data from the Central Bank of Kenya (CBK) reports and library.

This study adopted multiple - regression model which was:

$Y = \ + \ _1X1 + \ _2X2 + \ _3X3 + \ldots\ldots \ _4X_n + €$

Where

Y=Dependent variable (**Economic Growth**); Measured by the GDP and GNP X=Independent variable (**Financial Liberalisation**); where X_1= Credit controls; including Foreign Assets and directed credit toward favored sectors or industries,Ceilings on credit toward other sectors, and excessively high reserve requirements. X_2= Interest rate control; including Lending Interest Rates and cases where the government directly controls, Interest rates or where floors, ceilings, or interest rate bands exist.

X_3= Capital Controls; Restrictions on international financial transactions, including Current Account Performance and restrictions on capital and current account convertibility, and the use of multiple exchange rates. = Constant term. = Gradient/Slope of the regression measuring the amount of the change in Y associated with a unit change in X

€=Error term within a confidence interval of 5%

4.0 Data Analysis Findings and Discussions

The study findings are presented on the relationship between financial liberalization and economic development in Kenya. The study used secondary data from the Central Bank of Kenya (CBK) reports and library, The study sought to establish the trend of Economic Growth in Kenya over the study period. From the findings, the study established that Economic Growth had been on continuous

increase over the study period. The 2002/2003 financial year recorded an economic growth of 1,055,658 million shillings. This increased to 1,109,541 million shillings in 2003/2004, follow by a further increase to 1,175,133 shillings in 2004/2005 financial year. In the 2005/2006 financial year, economic growth increased to 1,249,470 million shillings, followed by further increase to 1,336,846 million and then 1,357,263 million shillings in the 2006/2007 and 2007/2008 financial year respectively. it is noted that the economic growth in 2006/2007 financial year was very slow. Economic Growth further increased to 1,394,387 million shillings in 2008/2009, followed by a further increase to 1,474,763 million shillings in 2009/2010 then 1,539,306 million shillings in 2010/2011. This implied that the economic growth of Kenya had been increasing over the study period however the study the growth was gradual as evidenced by the findings of this study. This study however notes that the economic growth was very slow in2006/2007 financial year as evidenced by the findings of this study.

Further the study sought to establish the trend in the lending interest rates over the study period, The study findings established that at the inception year 2003, the lending interest rates were 16.37%. These rates decreased in the year 2004 to 12.53%. Since then the study findings established that the lending interest rates have been on increase. In the year 2005 the lending interest rates were at 12.89% which increased gradually to 13.64% in the year 2006, before a slight decrease to 13.33% in 2007. In the year 2008, the interest rate increased to 14.02%, then to 14.08% in the year 2009 and further increase was recorded in the year 2010 whereby the lending interest rates was 14.36%. By the year 2011, the interest rates had increased to 15.05% after which in the year 2012, there was a rapid increase in lending interest rates whereby the rates increased to 19.65%.

The study also sought to determine the trend in foreign asset during the study

period. The traditional approach to measuring financial openness is to measure of the sum of gross stocks of foreign assets and liabilities as a ratio to a country‟s gross domestic product. From the findings, it was noted that foreign assets stood at USD. 110,991 million in the year 2003. Foreign assets increased thereafter to stand at USD. 115,774, 129, 248, 167,046 and 228,677 for the years 2004, 2005, 2006 and 2007 respectively. This shows that following financial liberalization, more investors were willing to move their investments into the country. After the year 2007, foreign investment dropped slightly in the year 2008 to USD 223,549before picking up a positive trend again from the year 2009 till 2012. The drop in the financial year 2008 could be attributed to the post election violence that rocked the country following the disputed presidential results. This situation caused political instability which forced foreign investors to relocate some of their investments.

However, after the peace deal was signed, the inflow of foreign assets continued to increase to USD 263,019, 321,118,359,652 and 374,457 for the years 2009, 2010, 2011 and 2012 respectively.

The study further sought to analyze the performance of the current account for Kenya over the study period. Positive current account balance measures the portion of a country's saving invested abroad while negative, the portion of domestic investment financed by foreign investment. From the findings, the current account started from a positive meaning that most of the country‟s savings were invested abroad. By the year 2003, the current account stood at positive USD 118 million. Starting the year 2004, the proportion of domestic investments financed by foreign capital started increasing. It stood at USD -2 million then continued increasing to USD -252 in the year 2005, -396 in the year 2006, to USD - 1964 by the year 2009. The amount of domestic investments financed by foreign assets has continued to increase to reach a high of USD 3,968 million by the year

African Journal Of Business And Management http://aibumaorg.uonbi.ac.ke/content/journal

Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

2012.

In order to establish the relationship among the variables (independent), multiple regression analysis was conducted. The analysis applied the statistical package for social sciences (SPSS) to compute the measurements of the multiple regressions for the study. The findings were as shown in the table 1 below

Table 1: Model Summary

Model Summary				
Model	R	R Squre	Adjusted R Square	Std Error of the Estimate
1	.991 a	0.983	0.974	29311.94531
a. Predictors: (constant), Lending rates(USD), Current Account				

Source: Research(2013

In order to explain the percentage of variation in the dependent variable (Economic Growth) that is explained by the independent variables, the researcher used coefficient of determination obtained from the model summary in table 4.1. Coefficient of determination explains the extent to which changes in the dependent variable (Economic Growth) can be explained by the change in the independent variables or the percentage of variation in the dependent variable that is explained by all the three variables (Lending rates, current account balance and foreign assets).

From the analysis, the independent variables (Lending rates, current account balance and foreign assets) in this study contributed to 98.3% of the variation in Economic Growth as explained by adjusted R^2 of 0.983.

The study conducted an Analysis of Variance, in order to test the significance of the model. The findings were as shown below:

African Journal Of Business And Management
http://aibumaorg.uonbi.ac.ke/content/journal

Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

Table 2: ANOVA Variance

ANOVA[b]						
Model		Sum of Squres	df	Mean Squres	F	Sig.
1	Regression	2.90E11	3	9.68E10	112.612	.000a
	Residual	5.16E09	6	8.59E08		
	Total	2.95E11	9			
a. Predictors: (constant), lending rates, Foreign Assets(USD), Current Acc						
b. Dependent Variable: Economic growth measures by GDP(Million Kshs)						

From the ANOVAs results, the probability value of 0.000 was obtained implying that the regression model was significant in predicting the relationship between Public Debt and the predictor variables as it was less than =0.05. By use of the F-table, the $F(5\%,3,6)$ tabulated was 4.7571 which was less that F= 112.612 which as well indicated that the model was significant.

Table 3: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1163591.839	133586.063		8.710	.000
	Foreign Assets (USD)	1.283	.395	.702	3.249	.017
	Current Account	-51.918	33.275	-.387	-1.560	.170
	Lending rates	-13514.612	7356.599	-.158	-1.837	.016
a. Dependent Variable: Economic Growth measures by GDP (Million Kenya Shillings)						

Author: Research data (2013)

The researcher conducted a regression analysis so as to determine how lending rates, foreign assets (USD) and current account (independent variables) contributes to economic growth (dependent variable). The following regression equation was obtained:

$$Y = 1163591.839 + 1.283X_1 - 51.918X_2 - 13514.612X_3 + €$$

From the regression model obtained above, holding all the other factors constant, the economic growth measures by GDP would be 1163591.839. A unit

change in foreign assets holding the other factors constant will lead to change the economic growth by 1.283; A unit change in current account holding the other factors constant will change economic growth by -51.918 while a unit change Lending rates holding the other factors constant will change economic growth by -13514.612. This implied that foreign assets had the highest influence on the economic growth followed by current account and finally lending rates

The obtained regression equation further implied that there was a direct relationship between economic growth

and foreign assets while the relationship between economic growth and current account together with lending rates was lending rates inverse.

The analysis was undertaken at 5% significance level. The criteria for comparing whether the predictor variables were significant in the model was through comparing the corresponding probability value obtained and =0.05. If the probability value was less than , then the predictor variable was significant otherwise it wasn"t. Foreign assets and lending rates were significant in the model as their corresponding predictor variables were 0.016 and 0.017 respectively while the current account performance was insignificant in the model as the probability value obtained was 0.170. Although Kenya is currently in a stage of growth, there are still several factors inhibiting economic development and contributing to the poverty trap. Economic growth in Kenya as found out in the study been evident over the study period as it grew continuously as from 2002/2003 financial year, were it was Ksh.1,055,658 million to reach a high of 1,539,306 million as at the end of 2010/2011 fiscal year

lending rates had been an increasing in the lending rates over the study period. The study findings established that in the year 2003, the lending rates were rates were 16.37%. These rates decreased in the year 2004 to 12.53%. Since then, the lending interest rates increased gradually to 19.65% by the year 2011. In the year 2012, there was a rapid increase in lending interest rates whereby the rates increased to 19.65%.

Foreign assets as found by the study had been increasing over the study period with exception of the 2008 financial year. Foreign assets stood at USD. 110,991 million in the year 2003. Foreign assets increased thereafter to stand at USD. 115,774. After the year 2007, foreign investment dropped slightly in the year 2008 to USD 223,549 before picking up a

positive trend again from the year 2009 till 2012 were it amounted to USD 374,457.

The study findings established that current account, the study established that it started from a positive meaning that most of the country"s savings were invested abroad. By the year 2003, the current account stood at positive USD 118 million. Starting the year 2004, the proportion of domestic investments financed by foreign capital started increasing. It stood at USD -2 million then continued increasing to USD -252 in the year 2005, -396 in the year 2006, to USD -1964 by the year 2009. The amount of domestic investments financed by foreign assets has continued to increase to reach a high of USD 3,968 million by the year 2012.

With regard to economic growth, the study findings established that the economic growth had been increasing continuously over the study period. At the 2002/2003 financial year, the economic growth as reflected by GDP was Ksh.1,055,658 million. This increased gradually over the years to Ksh.1,357,263 million in the 2006/2007 after which the growth rate decrease over the 2007/2008 and 2008/2009. As at the end of 2010/2011 fiscal year, the economic growth had increased further as shown by GDP of Ksh. 1,539,306 million.

On the lending rates the study findings established that there had been an increase in the lending rates over the study period. The study findings established that in the year 2003, the lending rates were t rates were 16.37%. These rates decreased in the year 2004 to 12.53%. Since then, the lending interest rates increased gradually to 19.65% by the year 2011. In the year 2012, there was a rapid increase in lending interest rates whereby the rates increased to 19.65%.

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Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

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By the year 2003, the current account stood at positive USD 118 million. Starting the year 2004, the proportion of domestic investments financed by foreign capital started increasing. It stood at USD -2 million then continued increasing to USD -252 in the year 2005, -396 in the year 2006, to USD -1964 by the year 2009. The amount of domestic investments financed by foreign assets has continued to increase to reach a high of USD 3,968 million by the year 2012.

The study findings established that there was a strong relationship between economic growth and the independent variables under study and that they greatly affected the variability of economic growth. The study findings established that there was a direct relationship between economic growth and foreign assets while the relationship between economic growth and current account together with lending rates was inverse.

The Central Bank was actively involved in several regional integration initiatives particularly those relating to monetary integration. The Bank participated in the implementation of monetary co-operation programmes of the East African Community (EAC), Common Market for Eastern and Southern Africa (COMESA) and the Association of African Central Banks (AACB).

From the study findings a strong relationship between economic growth and the independent variables existed. The study findings established that there was a direct relationship between economic

growth and foreign assets while the relationship between economic growth and current account together with lending rates was inverse.

5.0 Summary, Conclusions and Recommendation

5.1 Summary and Conclusions

The study concludes that economic development in Kenya is highly influenced by the financial liberalisation. lending interest rates, foreign investments as well as current account performance highly influence economic development. Further, the study concludes that economic growth had been on increase as indicated by the increase in GDP. The study further concludes that the political instability has a negative effect on the economic growth of the any economy.The study findings also concludes that lending rates have a detrimental impact on the economic growth. An increase in lending rates reduces the economic growth rate. The study further concludes that the lending rates have been on increase over the past years.

The study concludes that foreign assets positively influences economic growth as the there exists a direct relationships between the foreign assets and economic growth. The study further concludes that foreign assets have been increasing over the period of study and that instability discourages foreign assets in the country.The study concludes that the proportion of domestic investments financed by foreign capital has been increasing over years. in addition the study concludes that that most of the country‟s savings is invested locally compared to the previous year whereby was invested locally.The drop in the financial year 2008 could be attributed to the post election violence that rocked the country following the disputed presidential results. This situation caused political instability which forced foreign investors to relocate some of their investments. However, after the peace deal was signed, the inflow of foreign assets continued to increase to

USD 263,019, 321,118,359,652 and 374,457 for the years 2009, 2010, 2011 and 2012 respectively.

5.2 Recommendations for Further Research

The study has confirmed that the Central Bank of Kenya is very significant in enhancing the the Financial Liberalization phennomena. Which enables Economic Development.The study findings established that lending rates have increased continuously over the study period. Based on the inverse relationship existing between lending rates and economic growth as established by the study findings, this study calls upon for regulatory measures on the interest rates. Policy makers should come up with regulatory policies that regulate the lending rates. The institutions charged with regulation of interest rates should be capacitated with all the necessary support they need in order to execute the mandate of regulating their lending rates.

The study findings also established that economic growth rate reduced in 2008 as well as foreign assets. Since these this year had been marked with the post election violence that rocked the country following the disputed presidential results, this could be contributed to the changes in the trend. This study therefore recommends that there is need for policy makers to come up with polices that ensure that the election code of and ethics are upheld during elections. The study finally recommends that policy makers should enact rules that encourage and attract foreign investors into the country as well as discouraging investments of countries savings locally.

A comparative study can be carried out to establish whether financial liberalization in other countries is able to impact the economic development. Thus enabling comparison with the Kenyan experience and provide concrete facts upon which reliable conclusions can be made. Since economic growth is not affected by on lending rates, foreign assets and account performances, this study recommends that further studies be done to incorporates

other factors influencing the economic growth.The study findings established that economic development in Kenya was highly influenced by the financial liberalisation and that lending interest rates, foreign investments as well as current account performance highly influenced economic development. The study findings established that economic growth had been on increase as indicated by the increase in GDP as well as foreign assets and lending rates and that lending rates negatively affected the affected the economic development while foreign assets in positive influenced economic development. The study recommends that policy makers should come up with regulatory policies that regulate the lending rates and encourage and attract foreign investors into the country as well as discouraging investments of countries savings locally.

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Special Issue: Volume 4, Issue 3, October 2018 Pgs 53- 79

Appendices

Appendix I: Dataset on Foreign Assets, Lending rates and GDP

Period	Foreign Assets (USD)	Lending rates	Economic Growth measures by GDP (Million Kenya Shillings)
Year 2003	110991	16.6	1055658
Year 2004	115774	12.5	1109541
Year 2005	129248	12.9	1175133
Year 2006	167046	13.6	1249470
Year 2007	228677	13.3	1336846
Year 2008	223549	14.2	1357263
Year 2009	263019	14.8	1394387
Year 2010	321118	14.4	1474763
Year 2011	359652	15.1	1539306
Year 2012	374457.19	19.7	1597198

Current Account Performance in Kenya 2003-2012

Period	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual Average
Year 2003	90	81	142	99	102	100	83	88	146	157	184	145	118
Year 2004	128	72	0	18	35	27	61	13	-104	-71	-67	-133	-2
Year 2005	-257	-186	-85	-287	-257	-283	-236	-336	-253	-305	-291	-253	-252
Year 2006	-234	-333	-401	-407	-465	-376	-386	-322	-376	-425	-521	-511	-396
Year 2007	-540	-644	-644	-484	-481	-613	-788	-787	-851	-965	-1009	-1034	-737
Year 2008	-1207	-1046	-1116	-1090	-1234	-1175	-1242	-1535	-1745	-1820	-1876	-1973	-1421
Year 2009	-1889	-2032	-1973	-2166	-2167	-2260	-2204	-1925	-1856	-1740	-1678	-1671	-1964
Year 2010	-1720	-1625	-1760	-1723	-1851	-1920	-1974	-2017	-2073	-2147	-2408	-2512	-1978
Year 2011	-2492	-2551	-2589	-2552	-2718	-2800	-2823	-3164	-3171	-3107	-3190	-3330	-2874
Year 2012	-3399	-3503	-3768	-3892	-3853	-3895	-4181	-4150	-4284	-4352	-4121	-4221	-3968