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Rodah Nyanchera Gekonge & Dr. Julius Miroga, PhD



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FIRM CHARACTERISTICS AND FINANCIAL PERFORMANCE OF MICRO-FINANCE INSTITUTIONS IN ELDORET CITY, KENYA

Rodah Nyanchera Gekonge¹ & Dr. Julius Miroga, PhD²

¹ MBA (Finance) Student, Jomo Kenyatta University of Agriculture and Technology, Kenya ² Lecturer, Jomo Kenyatta University of Agriculture and Technology, Kenya

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ABSTRACT

This study investigated the relationship between firm-specific characteristics and the financial performance of microfinance institutions operating within Eldoret City, Kenya. More precisely, the research focused on examining how key factors namely, board size, loan portfolio quality, firm leverage and firm liquidity on the institution's financial performance. The study targeted population of 143 employees in 4 DTMs in Uasin Gishu County. The findings of the research demonstrated that several organizational characteristics, specifically firm leverage, liquidity levels, the size of the loan portfolio, and the number of board members, exert a measurable influence on the financial performance of MFIs operating within Eldoret City, Kenya. Furthermore, the analysis indicated that each of the independent variables exhibited a statistically significant and positive correlation with the dependent variable, financial performance. The outcomes of the linear regression model further confirmed the existence of a strong and meaningful association between the firmspecific attributes and the financial outcomes of the MFIs. It was concluded that that MFIs that strategically use leverage by acquiring debt to finance their operations tend to experience improved financial outcomes; MFIs with higher liquidity levels are better positioned to meet short-term obligations, sustain operational efficiency, and seize investment opportunities that drive profitability; MFIs that expand their loan portfolios improve their financial performance improves; and larger boards contribute positively to financial outcomes leading to improved governance mechanisms. It was recommended that MFIs should continuously assess their leverage ratios to maintain optimal capital structures that support long-term profitability, and should strengthen their liquidity management practices to achieve long-term growth. Policymakers and financial regulators should also support MFIs by providing an enabling environment that promotes responsible lending practices, effective credit risk management, and regulatory compliance.

Key Words: Board Size, Loan Portfolio Quality, Firm Leverage, Firm Liquidity

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INTRODUCTION

Microfinance has emerged as a critical tool for empowering low-income individuals, particularly those who have been historically marginalized by financial mainstream institutions such ลร commercial banks and formal lending agencies. According to Gheysari et al. (2016), microfinance initiatives aim to build the economic capacities of the poor by facilitating access to essential financial services, including loans, savings opportunities, and insurance products. Through these interventions, beneficiaries are gradually supported to transition into sustainable self-employment and entrepreneurial activities.

Traditionally, microfinance has been closely intertwined with microcredit, referring to the provision of small loans extended without conventional collateral requirements. As noted by Gamble and Blackwell (2018), such credit programs have predominantly targeted individuals and families facing acute subsistence challenges, especially in developing nations, with the dual objective of enhancing household livelihoods and sustaining small-scale economic ventures.

The evolution of the microfinance sector has further underscored the economic potential of lowincome earners, demonstrating that they constitute a viable and profitable customer segment when approached with appropriate financial models. However, achieving this viability necessitates the management of effective risks commonly associated with lending, such as moral hazard, adverse selection, and other agency-related challenges (Fill, 2017; Fenwick, 2016; Eze et al., 2019). By addressing these risks, microfinance institutions are better positioned to ensure both the sustainability of their operations and the financial inclusion of underserved populations.

MFIs have played a key role in advancing financial inclusion, predominantly among low-income populations, thereby contributing significantly to poverty reduction efforts. According to Wei (2018), one of the critical factors influencing the performance of microfinance organizations is their liquidity position. Sufficient liquidity enables these institutions to swiftly convert their assets into cash, allowing them to meet client demands effectively, especially during periods of economic uncertainty or crises when conventional banks might limit or suspend their operations. Despite the notable growth and expansion of the microfinance sector, MFIs continue to grapple with several persistent challenges. Among these, a major obstacle is their limited access to long-term financing options, which has been shown to negatively affect their overall profitability (Dongmei et al., 2022).

Scholars have underscored the importance of strengthening capital structures and managing liquidity risks prudently to enhance the performance of both microfinance institutions and banks. Maintaining adequate cash reserves while avoiding excessive liquidity exposure is essential for sustaining financial health (Sekabira, 2013; Arif & Anees, 2012). Additionally, supportive government policies have been instrumental in facilitating the growth of the microfinance sector. In Kenya, for instance, favourable cash reserve ratio regulations set by the Treasury have played a key role in broadening the reach of microfinance services to underserved communities (Chirchir, 2020).

Furthermore, microfinance institutions address the unique financial needs of low-income groups through tailored solutions such as group lending mechanisms and relaxed collateral requirements. By offering these alternative financing models, MFIs effectively bridge the gaps left by traditional banking systems (CGAP, 2017). Integrating such innovative approaches with formal banking structures holds the potential to deepen financial inclusion, ultimately generating significant socioeconomic benefits for marginalized populations.

MFIs in Kenya face a range of challenges that impact their financial performance. These challenges stem from both external factors in the economic environment and internal management inefficiencies. One of the major challenges MFIs in Kenya face is the high level of non-performing loans (NPLs) or defaults. Many borrowers are either unable or unwilling to repay their loans due to economic hardships, poor financial literacy, or overindebtedness. The rural and urban poor, the primary clients of MFIs, often face unstable incomes, making loan repayment difficult (Muthoni & Njuguna, 2021). MFIs require a stable source of capital to sustain their lending operations. However, many face difficulties in accessing funds from traditional banking institutions. This issue is exacerbated by a relatively underdeveloped financial infrastructure and a lack of trust from larger banks (Kinyua & Waweru, 2022).

Regulatory constraints and the cost of compliance are significant hurdles for MFIs in Kenya. The government and the Central Bank of Kenya (CBK) have put in place stringent measures to regulate the financial sector, which often increases the operational costs of MFIs. Many smaller institutions find it hard to meet these regulatory requirements, particularly with respect to capital adequacy and reporting standards (Wanjiru & Kamau, 2020). With the entry of commercial banks and mobile lending platforms such as M-Shwari, MFIs face increasing competition. Mobile platforms offer more flexible loan terms and faster processing times, leading to a shift in customer preferences away from traditional MFIs (Gichanga & Mwangi, 2022).

Majority of the MFIs are also facing operational Inefficiencies due to inadequate financial management, weak internal controls, and a lack of skilled human resources hamper operational performance, thus limiting financial growth and sustainability (Muturi & Otieno, 2023). Many MFI clients take loans from multiple institutions, leading to over-indebtedness. This puts strain on their ability to repay loans, ultimately affecting the financial health of MFIs as they experience higher default rates (Ochieng & Wanyama, 2023). It is against this background that the study will be conducted to investigate the relationship between firm characteristics and financial performance of MFIs in Eldoret City, Kenya.

Statement of the Problem

MFIs were in Kenya were originally established with the primary goal of providing financial assistance to individuals with low income who traditionally lacked access to formal credit facilities. By offering more accessible services and building a wider network compared to conventional banking institutions, MFIs succeeded in extending loans to underserved populations. However, despite this initial success, the majority of microfinance institutions in Kenya have been grappling with financial losses since the CBK issued the first operational license in 2009. The global financial crisis, which unfolded between mid-2007 and early 2009, emphasised the urgent need for regulatory oversight in the microfinance sector to mitigate the significant risks associated with financial instability and institutional imbalances. Furthermore, the Central Bank of Kenya's 2019 Bank Supervision Annual Report revealed that many MFIs in the country collapsed as a result of ineffective credit risk management strategies. This failure was particularly evident in the rising levels of NPLs, which strained their financial sustainability and operational viability.

Between 2016 and 2020, MFIs in Kenya experienced a troubling downward trend in their financial performance. In 2016, the sector recorded an average decline in both ROA and ROE, with ROA falling by 0.5% and ROE dropping by 3.2%. The situation worsened in 2017, as the average ROA slipped further to -0.9%, while ROE declined more steeply to -5.5%. This negative trajectory continued into 2018, when ROA deteriorated to -2% and ROE plummeted significantly to -13.8%. A slight recovery was noted in 2019, with ROA improving marginally to -0.4% and ROE reducing its loss to -3%. However, this improvement was short-lived; in 2020, financial performance fell sharply once again, as ROA declined to -3% and ROE to a concerning -28% (CBK, 2021). These figures demonstrate not only a persistent decline but also considerable volatility in the profitability of MFIs over the five-year period. Despite various strategies implemented to mitigate

financial risks during this time, the sector's performance remained unstable and unpredictable. Consequently, it remains unclear whether inherent firm characteristics play a significant role in influencing the financial outcomes of MFIs, given the sustained challenges and fluctuations observed.

Previous research has explored the relationship between firm characteristics and the financial performance of MFIs, yet several limitations remain. For example, Biter et al. (2018) investigated the influence of capital ratios on the profitability of firms within OECD countries. However, the unique operational environments and policy frameworks in developing nations raise concerns about the applicability of these findings to such contexts. In another study conducted in Nigeria, Dioha et al. (2018) analyzed the link between capital structure and the performance of banks. Nonetheless, their research overlooked other critical factors that could also play a pivotal role in determining financial outcomes. Additional evidence of research gaps emerges from studies that have concentrated narrowly on specific variables while neglecting others of equal importance. Noor (2020), for instance, focused exclusively on examining the equity impact of financing on financial performance, while Nwankwo (2019) centered his investigation on the role of capital adequacy as a key driver of bank performance. Collectively, these studies highlighted a fragmented approach, with each emphasizing different aspects of firm characteristics but leaving out integral variables related to the microfinance sector.

Objectives of the Study

The main objective was to establish the relationship between firm characteristics and financial performance of MFIs in Eldoret City, Kenya. The specific objectives were;

- To find out the effect of firm leverage on financial performance of MFIs in Eldoret City-Kenya.
- To establish the effect of firm liquidity on financial performance of MFIs in Eldoret City-Kenya.

- To assess the effect of loan portfolio on financial performance of MFIs in Eldoret City-Kenya.
- To determine the effect of board size on financial performance of MFIs in Eldoret City-Kenya

The study was guided by the following research hypotheses

- H_{o1} There is no significant relationship between firm leverage and financial performance of MFIs in Eldoret City- Kenya
- H₀₂ There is no significant relationship between firm liquidity and financial performance of MFIs in Eldoret City, Kenya.
- H₀₃ There is no significant relationship between loan portfolio and financial performance of MFIs in Eldoret City, Kenya
- H₀₄ There is no significant relationship between board size and financial performance of MFIs in Eldoret City, Kenya

LITERATURE REVIEW

Theoretical Review

Modern Portfolio Theory

Modern Portfolio Theory (MPT), introduced by Harry Markowitz in 1952, emphasizes the importance of constructing investment portfolios that achieve the best possible balance between risk and return. According to this theory, investors or organizations should aim to optimize their portfolios in such a way that they obtain the maximum expected returns for a specific and predetermined level of market risk. In essence, MPT advocates for selecting a combination of assets that not only diversifies investment but also ensures that the return achieved is the highest attainable without exceeding the investor's risk tolerance. Markowitz's framework laid the foundation for understanding how diversification can reduce overall portfolio risk while maintaining or enhancing returns (Markowitz, 1952).

The theory further emphasizes the concept of loan diversification as a critical strategy for mitigating risk by holding a broad range of assets that do not move in tandem (Kahneman & Tversky, 1979). The underlying principle is that the individual risks associated with each asset can offset one another, ultimately decreasing the total risk exposure within the portfolio. Markowitz's MPT builds on this notion by providing a quantitative framework that demonstrates how combining assets with low or negative correlations can lead to a reduction in overall portfolio risk (Sortino & Satchell, 2001). According to MPT, diversification does not merely spread investments but strategically aligns them to balance risk and reward. The theory guides investors to construct portfolios that achieve the optimal balance between expected returns and acceptable risk levels. By allocating investments across a variety of uncorrelated assets, it becomes possible to minimize risk while maintaining or even enhancing potential returns. In essence, MPT advocates for a deliberate diversification approach that enables investors to manage risk more effectively without necessarily compromising the portfolio's performance.

Trade-Off Theory

The trade-off theory explains that a firm determines its optimal mix of debt and equity financing by weighing the advantages against the drawbacks of each option. Kraus and Litzenberger (1973), who were the pioneers in formalizing this theory, proposed that companies aim to strike a balance between the benefits of tax shields provided by debt and the potential costs associated with bankruptcy and agency problems. Specifically, since interest payments on debt are deductible from taxable income, firms can use debt strategically to lower their tax obligations. Nevertheless, while debt can be beneficial in reducing taxes, it simultaneously increases a firm's financial risk exposure, raising the likelihood of encountering financial distress if not managed prudently.

According to Niu (2018), corporate managers perceive the choice between debt and equity as a balancing act between the tax savings achieved through debt financing and the accompanying costs of leverage, such as bankruptcy risks, agency costs, and the reduction of other non-debt tax shields. The theory suggests that firms aspire toward an ideal or target debt-to-equity ratio and make gradual adjustments over time to reach that equilibrium. Moreover, the trade-off theory predicts that firms with higher profitability are more inclined to take on additional debt because they possess stronger capacity to service debt and can benefit more from tax shields due to their higher taxable earnings. Conversely, firms with significant growth prospects are expected to maintain lower debt levels to avoid the heightened risks of financial distress that could jeopardize future opportunities; these firms are more likely to depend on equity financing to support their expansion plans.

Agency Cost Theory

Agency Cost Theory, initially introduced by Stephen Ross and Barry Mitnick in 1970 and later developed further by Jensen and Meckling in 1976, explains the inherent challenges that arise when there is a division between ownership and managerial control within an organization. According to this theory, when the individuals who own the firm (the shareholders) are not the same as those who manage its daily operations (the managers), a conflict of interest may emerge. Managers, acting as agents on behalf of the shareholders, may prioritize their own personal goals and interests rather than focusing solely on maximizing shareholder wealth. As a result, managers might engage in decisions that serve their own preferences, such as allocating resources for personal perks, selecting projects based on their own agendas, or making operational choices that deviate from the optimal path for increasing the firm's overall value.

Berger (2002) describes agency costs as the reduction in firm value stemming from such managerial behaviors where professional managers prioritize their own satisfaction over the objective of maximizing shareholder returns. In essence, these costs represent the inefficiencies created when managers pursue self-serving actions rather than aligning with the interests of the owners. The theory further suggests that increasing a firm's level of debt, or financial leverage, can serve as a mechanism to curb such agency problems. Highly leveraged firms, according to the agency cost hypothesis, are better positioned to limit the discretionary power of managers since debt obligations impose stricter discipline on managerial decisions, thereby enhancing organizational performance and ultimately boosting firm value. Myers (1977) also supports this view by arguing that a higher reliance on debt financing can help mitigate the conflicts that typically arise between managers and shareholders, especially regarding investment choices. Therefore, the theory emphasizes that an organization's capital structure plays a crucial role in managing agency costs and can have a significant impact on the firm's performance and value creation (Berger, 2002).

The theory also sheds light on how leverage decisions can be influenced in order to address agency conflicts that emerge within a firm. In addition to this, it provides insight into the essential role that corporate governance, specifically the board of directors, plays in overseeing the actions of managers, who often act as agents of the shareholders. According to Fama and Jensen (1983), the board is crucial in holding managers accountable, ensuring that their actions align with the goal of maximizing shareholder wealth, rather than prioritizing their personal interests. The board's primary function is to monitor the internal managers closely and act as a safeguard to prevent any conflicts of interest that could harm the financial well-being of the firm. As a result, the larger the size of the board of directors, the more robust its ability to provide effective oversight and

mitigate potential risks associated with managerial self-interest.

Liquidity Preference Theory

The Liquidity Preference Theory was introduced by John Maynard Keynes in 1930. In this theory, Keynes argued that the rate of interest is fundamentally influenced by the interaction between the supply of money and the demand for liquidity. He posited that interest is essentially a monetary concept, reflecting the reward required by individuals for forgoing liquidity over a specific time horizon. Rather than viewing interest as the price that balances the demand for investment resources with the willingness to postpone consumption, Keynes emphasized that it serves as the price that aligns people's preference for holding their wealth in liquid form—cash—with the amount of money actually available in the economy. In other words, interest equilibrates the desire to retain cash balances with the existing money supply.

Expanding on liquidity challenges, Kiplagat and Kalui (2020) defined liquidity risk as the predicament faced by market participants when they are unable to transform assets or stocks into cash immediately. This difficulty often arises during periods of liquidity shortages in the financial system due to structural and infrastructural or inefficiencies that hinder smooth transactions. Such conditions create obstacles for converting assets into liquid funds without incurring significant losses or delays, potentially affecting market stability and financial operations.

The theory is important to this study since MFIs are in need of money to keep the company's activities going therefore liquidity has an impact on their financial performance. They prefer to keep their resources liquid in order to enhance their financial performance and the supply of money comes from banks and the government with some interest. The MFIs keep cash in reserve to meet unexpected needs since according to Keynes people like to hoard money because it possesses liquidity. In addition, high interest rates are likely to curb business investments and innovation.

Empirical Review of Literature

Onsase and Irungu (2024) conducted a study to examine the impact of capital structure on the financial performance of deposit-taking microfinance banks in Nairobi City County, Kenya. The research utilized a descriptive research design to assess the situation. The study considered the full population of 13 licensed microfinance banks within Nairobi County. Secondary data was sourced from a variety of reputable organizations, and was subsequently analysed using SPSS. The results of the analysis revealed that equity capital significantly influences the performance of these MFIs. The study concluded that a strong capital structure, along with prudent management of equity, is essential for the effective functioning and sustainability of microfinance institutions. In terms of recommendations, the study urged these institutions to focus on capital adequacy planning, shift their attention towards areas that will have the greatest impact on their operations, and improve their debt management strategies in order to boost their overall performance. However, one limitation of the study is that its findings are primarily applicable to Nairobi and may not be directly transferable to Eldoret or other regions due to geographical differences.

Smith and Williams (2021) carried out research aimed at investigating the impact of liquidity management on the financial performance of microfinance institutions (MFIs) operating within the United States. Their study involved a sample of 50 MFIs drawn from various regions across the country. Utilizing secondary data extracted from the financial statements of these institutions over a five-year period spanning from 2015 to 2020, the researchers analyzed the link between liquidity management and financial outcomes. To achieve they applied correlation analysis and this, regression techniques, to evaluate how liquidity ratios related to critical measures of financial performance, specifically ROA and ROE. The study's

findings demonstrated a significant and positive effective association between liquidity management practices and improved financial performance among the MFIs included in the sample. Put differently, the results indicated that MFIs maintaining higher liquidity ratios were more likely to achieve superior returns in both assets and equity. This strong liquidity position enabled the institutions to meet their short-term liabilities promptly, thereby fostering confidence among both lenders and clients. However, it is important to note that the study was conducted in the context of the United States, a developed economy, whereas the present study will be situated in Kenya, a developing country. Additionally, while Smith and Williams (2021) focused exclusively on ROA and ROE as measures of financial performance, the current research intends to expand the scope by including profitability alongside ROA and ROE.

Loan portfolio management plays a critical role in enabling MFIs to meet their targeted loan portfolio outcomes. However, many MFIs have struggled to attain these planned performance levels. A number of them have encountered serious challenges not only generating dissatisfaction among their client base, but also failing to recover significant portions of disbursed loans, with some ultimately being forced to shut down operations. Such setbacks have negatively impacted their overall organizational performance, as a growing number of loans become delinquent. Consequently, MFIs are unable to fulfil their fundamental mission of extending financial services to individuals who remain excluded from the mainstream formal financial system. This situation has further eroded their profitability, thus reducing their revenue streams while simultaneously leaving them financially burdened by the need to cover ongoing operational and administrative expenses, including salaries for These personnel managing the institutions. challenges may be attributed to several factors, such as inadequate loan portfolio planning, insufficient vetting or evaluation of prospective borrowers (client screening/evaluation), and weak mechanisms for ensuring that the loans are used productively and repaid on time (loan portfolio control). Without robust systems for planning, monitoring, and enforcing loan repayment, MFIs are exposed to significant financial and operational risks. Therefore, in order for MFIs to enhance their performance and sustain their operations, it is imperative that they adopt effective strategies and practices for managing their loan portfolios. Doing so will not only safeguard their financial viability but also enable them to continue providing essential financial services to underserved populations.

Board size, which denotes the total number of directors serving on a company's board, is widely recognized as an influential factor in determining a firm's financial performance. However, scholarly opinions and research findings regarding its impact remain divided. On one hand, the Capital Markets **Conceptual Framework** Authority (CMA) recommends that companies adopt smaller board sizes, emphasizing that a board enhances leaner communication expedites effectiveness and decision-making processes. According to the CMA, larger boards often face challenges such as internal conflicts and prolonged deliberations, which can hinder swift and cohesive decision-making. Conversely, a study conducted by Orozco, Vargas, and Galindo-Dorado (2018) suggested that having more directors on the board could actually be advantageous, as it contributes positively to a firm's reputation and, by extension, its overall performance. Nonetheless, other researchers have argued the opposite, asserting that increasing the number of board members negatively impacts financial outcomes, primarily due to inefficiencies and coordination difficulties inherent in managing larger groups.



METHODOLOGY

Figure 1: Conceptual Framework

In this study, a correlational research design was adopted to investigate the relationship between various firm characteristics and their financial performance. For the purpose of this study, the research population was composed of all MFIs in Eldoret City, Kenya that had adopted deposit-taking hence transforming into Deposit Taking MFIs (also referred to as DTMs). In this case therefore, the targeted DTMs were Kenya Women Finance Trust (KWFT) PLC, Faulu Microfinance Bank, SMEP Microfinance Bank Limited, and Rafiki Microfinance Bank Limited. A total population of 143 employees work in the four DTMs in Uasin Gishu County. The researcher utilized Yamane's 1967 formulae to determine the sample size of 106 respondents.

The research study employed primary data collection method whereby a questionnaire was adopted as a data collection instrument as it allows the collection of data from a large population (Mugenda & Mugenda, 2003). The questionnaire contained closed-ended items rated on a five-point Likert-type scale containing SA (strongly agree), A (agree), U-undecided, D-disagree and SD (strongly disagree). The questionnaire was divided in five sections. The first section consists of the demographic characteristics of the employees, the second section: Firm leverage; third section: Firm liquidity; fourth section: Loan portfolio size; and last section: board size.

The data collected from the questionnaires were analysed and presented in terms of descriptive and inferential statistics. Descriptive statistics was used to analyse quantitative data and presentation done in tables and figures. SPSS version 27 was used for data analysis. To achieve this, responses obtained were first be tallied, percentages of variations computed and then described and interpreted based on the assumptions and the objectives of the study. Data was presented using tables, and pie charts to make them reader friendly. Regression method of analysis was used as the main statistical method. The regression model is expressed in the equation below.

 $Y = βo + β_1X_1 + β_2X_2 + β_3X_3 + β_4X_4 + ε.....(i)$

Where:

Y = Financial Performance
X1=Firm Leverage
X2 = Firm Liquidity
X3 = Loan Portfolio
X4= Board Size
βo = Intercept

 β = Coefficient of independent variables \notin = error term.

FINDINGS AND DISCUSSION

Response Rate

A total of 106 questionnaires were distributed to the selected respondents for this study. Out of these, 87 were completed and returned, resulting in a response rate of 82.1%. According to Mugenda and Mugenda (2003), a response rate of 70% or higher is considered sufficient for conducting a meaningful analysis of research findings. This high response rate indicated strong participant engagement and enhances the reliability of the collected data for drawing valid conclusions.

Descriptive Statistics

This subsection presents the descriptive statistics for each of the variables used in the study. A 5point Likert scale was used to assess the findings.

Firm Leverage

The respondents indicated the extent to which they agreed with various statements regarding the effect of firm leverage on financial performance of MFIs in Eldoret City, Kenya. They strongly agreed that the MFIs experience challenges in repaying outstanding debts on time (M=4.05, SD= 0.741); and the MFIs effectively manage debt repayment obligations without financial distress (M=4.01, SD=0.777). The respondents also agreed that High financial leverage has positively impacted the MFIs profitability and growth (M=3.75, SD=0.693), the MFIs maintain optimal levels of financial leverage to enhance financial performance (M=3.11, SD=0.504), and the MFIs rely on debt financing as a primary source of capital (M=3.26, SD=0.715). The respondents neither agreed nor disagreed that the MFIs have easy access to debt financing from financial institutions (M=2.92, SD=0.617). Generally, the respondents agreed that firm leverage affects financial performance of MFIs in Eldoret City, Kenya (M=3.47, SD=0.671). Table 1 summarises the findings:

Table 1: Firm Leverage

Statement	1	2	3	4	5	М	SD
The micro-finance institution has easy access	29.3%	20.0%	20.0%	18.7%	12.0%	2.92	.617
to debt financing from financial institutions.							
The micro-finance institution relies on debt	11.0%	13.7%	10.3%	26.0%	39.0%	3.26	.715
financing as a primary source of capital.							
Micro-finance institution experiences	9.3%	10.7%	16.0%	33.3%	41.3%	4.05	.741
challenges repaying outstanding debt on time.							
The micro-finance institution effectively	3.3%	6.7%	8.0%	42.0%	40.0%	4.01	.777
manages its debt repayment obligations							
without financial distress.							
The micro-finance institution maintains an	20.0%	18.7%	12.0%	29.3%	20.0%	3.11	.504
optimal level of financial leverage to enhance							
its financial performance.							
High financial leverage has positively impacted	8.0%	12.0%	8.0%	41.3%	30.7	3.75	.693
the institution's profitability and growth.							
Average						3.52	.675

Firm Liquidity

The respondents indicated the extent to which they agreed with various statements regarding the effect of firm liquidity on financial performance of MFIs in Eldoret City, Kenya. They agreed that the MFIs liquidity ratios (e.g., current ratio, quick ratio) indicate strong financial health (M=3.99, SD=0.601); the MFIs regularly review and optimize their current assets to improve liquidity (M=3.93, SD=0.840); the MFIs effectively manage their current liabilities to avoid liquidity risks (M=3.92, SD=0.729); the MFIs have a well-structured repayment schedule for its short-term obligations (M=3.88, SD=0.466); the MFIs maintain sufficient current assets to cover short-term obligations (M=3.80, SD=0.622); and the MFIs frequently assess liquidity ratios to ensure financial stability (M=3.75, SD=0.693). Overall, the respondents agreed that firm liquidity affect the financial performance of MFIs in Eldoret City, Kenya (M=3.88, SD=0.659). Table 2 summarises the findings:

Table 2: Firm Liquidity

Statement	1	2	3	4	5	М	SD
The micro-finance institution maintains	4.0%	10.7%	20.0%	32.0%	33.3%	3.80	.622
sufficient current assets to cover its short-							
term obligations							
The micro-finance institution regularly reviews	5.3%	14.7%	8.0%	25.3%	46.7%	3.93	.840
and optimizes its current assets to improve							
liquidity							
Micro-finance institution effectively manages	0.0%	14.7%	12.0%	33.3%	38.7%	3.92	.729
its current liabilities to avoid liquidity risks							
The micro-finance institution has a well-	0%	13.3%	22.7%	26.7%	37.3%	3.88	.466
structured repayment schedule for its short-							
term obligations							
The micro-finance institution's liquidity ratios	1.4%	12.0%	13.3%	33.3%	40.0%	3.99	.601
(e.g., current ratio, quick ratio) indicate strong							
financial health							
The micro-finance institution frequently	8.0%	12.0%	8.0%	41.3%	30.7	3.75	.693
assesses its liquidity ratios to ensure financial							
stability							
Average						3.88	.659

Loan Portfolio

Table 3: Loan Portfolio

The respondents indicated the extent to which they agreed with various statements regarding the effect of loan portfolio on financial performance of MFIs in Eldoret City, Kenya. They strongly agreed that the MFIs have well-defined creditworthiness assessment framework to evaluate loan applicants (M=4.37, SD=1.192); and has an efficient loan approval process that enhances timely disbursement of funds (M=4.17, SD=.888). The respondents agreed that the use of advanced credit-scoring models has improved loan portfolio quality (M=3.97, SD=0.721); loan approval decisions are based on clear and well-documented policies (M=3.97, SD=0.721); portfolio risk assessment helps in minimizing NPLs (M=3.92, SD=0.729); and the MFIs regularly conduct risk assessment to mitigate loan default risks (M=3.11, SD=0.504). Generally, the respondents agreed that loan portfolio affect financial performance of MFIs in Eldoret City, Kenya (M=3.23, SD=0.773). Table 3 summarises the findings:

Statement	1	2	3	4	5	Μ	SD
The micro-finance institution	0%	7.0%	13.3%	15.7%	64.0%	4.37	1.192
has a well-defined							
creditworthiness assessment							
framework to evaluate loan							
applicants							
The use of advanced credit-	2.7%	6.7%	20.0%	32.0%	38.7%	3.97	.721
scoring models has improved							
Ioan portfolio quality			40.00/		AA AA		
The micro-finance institution	20.0%	18.7%	12.0%	29.3%	20.0%	3.11	.504
regularly conducts risk							
default ricks							
Portfolio rick assessment helps	0.0%	1/1 7%	12 0%	33.3%	38 7%	3 0 2	720
in minimizing non-nerforming	0.070	14.770	12.070	55.570	50.770	5.52	.725
loans							
The micro-finance institution	1 3%	6 7%	6 7%	44 0%	<i>4</i> 1 3%	4 17	888
has an efficient loan approval	1.570	0.770	0.770	44.070	41.570	4.17	.000
process that enhances timely							
disbursement of funds.							
Loan approval decisions are	2.7%	6.7%	20.0%	32.0%	38.7%	3.97	.721
based on clear and well-							
documented policies.							
Average						3.23	.773

Board Size

The respondents expressed their level of agreement with various statements concerning board influences how size the financial performance of microfinance institutions (MFIs) in Eldoret City, Kenya. They strongly agreed that holding board meetings frequently enhances financial oversight and improves risk management within MFIs (M=4.17, SD=0.754). Additionally, they strongly agreed that having board members with

higher academic qualifications contributes to better financial decision-making in MFIs (M=4.11, SD=0.888). The respondents also agreed that board diversity — in aspects such as gender and professional expertise — positively impacts the financial performance of MFIs (M=3.99, SD=0.511). They agreed that the frequency of board meetings has a positive effect on the financial outcomes of MFIs (M=3.98, SD=0.704). Furthermore, they agreed that the presence of board members with financial expertise supports stronger financial performance in MFIs (M=3.93, SD=0.717). They also agreed that having a larger board size enhances strategic decision-making within MFIs (M=3.88, SD=0.654). Overall, respondents strongly agreed

Table 4: Board Size

that board size plays a role in influencing the financial performance of MFIs in Eldoret City, Kenya (M=4.01, SD=0.705). Table 4 summarises the findings:

Statement	1	2	3	4	5	М	SD
Greater diversity on the board,	1.3%	12.0%	13.3%	33.3%	40.0%	3.99	.511
including differences in gender							
and professional expertise,							
contributes to improved							
financial outcomes for MFIs.							
Having a larger number of board	0%	13.3%	22.7%	26.7%	37.3%	3.88	.654
members promotes more							
effective strategic decisions							
within MFIs.							
Holding board meetings more	10.7%	9.3%	16.0%	33.3%	41.3%	4.17	.754
regularly strengthens financial							
supervision and enhances risk							
management in MFIS.	7.00/	7.00/	7.00/	24 40/		2.00	704
An increased number of board	7.8%	7.8%	7.9%	31.4%	45.1%	3.98	.704
meetings has a positive impact							
The presence of board members	0%	12 0%	12 2%	11 0%	20.7%	2 0 2	717
with financial knowledge and	070	12.070	13.370	44.070	30.770	3.33	./1/
skills helps boost the financial							
performance of MEIs							
Board members with advanced	1.3%	6.7%	6.7%	44.0%	41.3%	4.11	.888
educational backgrounds	,	••••	••••				
enhance the quality of financial							
decision-making in MFIs.							
Average						4.01	.705

Financial Performance of MFIs

The respondents indicated the extent to which they agreed with various statements regarding the financial performance of MFIs in Eldoret City, Kenya. They strongly agreed that the MFIs have experienced steady growth in profitability over the last three years (M=4.06, SD= 0.817), and the return on equity of our micro-finance institution has shown a positive trend over the past three years (M=4.01, SD= 0.611). The respondents agreed that

the return on assets of the MFIs have consistently improved over the past three years (M=3.98, SD=0.704); the MFIs effectively utilize assets to generate profits (M=3.92, SD=0.677); the MFIs efficiently use shareholders' equity to generate profits (M=3.63, SD=0.557); and profitability ratios indicate that the MFIs are financially sustainable (M=3.59, SD=0.765). Table 5 summarises the findings:

Table 5: Financial Performance of MFIs

Statement	1	2	3	4	5	М	SD
Our micro-finance institution	5.9%	25.5%	17.7%	7.8%	43.1%	3.92	.677
effectively utilizes its assets to							
generate profits							
The return on assets of our	7.8%	7.9%	7.9%	31.3%	45.1%	3.98	.704
micro-finance institution has							
consistently improved over the							
past three years							
Our micro-finance institution	13.5%	4.1%	15.5%	27.5%	39.4%	3.63	.557
efficiently uses shareholders'							
equity to generate profits							
The return on equity of our	4.0%	10.7%	10.0%	42.0%	33.3%	4.01	.611
micro-finance institution has							
snown a positive trend over the							
Our micro finance institution	F 00/	F 00/	12 70/		40.00/	4.00	017
bas experienced steady growth	5.9%	5.9%	13.7%	23.3%	49.0%	4.00	.617
in profitability over the last							
three years							
Profitability ratios indicate that	2.0%	10 7%	23 5%	30.2%	24.6%	2 50	765
our micro-finance institution is	2.070	10.770	23.370	39.270	24.070	3.39	.705
financially sustainable							
Average						3.84	.704

Inferential Statistics

Correlation Analysis

The study used Spearman rank correlation to analyse the relationship between the independent

variables (Firm Leverage, Firm Liquidity, Loan Portfolio, and Board Size) and the dependent variable (Financial Performance of MFIs). Table 6 summarises the findings.

		Financial	Firm	Firm	Loan	Board
		Performance	Leverage	Liquidity	Portfolio	Size
Financial	Pearson	1				
Performance	Correlation					
	Sig. (2-					
	tailed)	87				
	Ν					
Firm Leverage	Pearson	.715*	1			
	Correlation					
	Sig. (2-	.023	.000			
	tailed)	87	87			
	Ν					
Firm Liquidity	Pearson	.856*	.711	1		
	Correlation					
	Sig. (2-	.000	.000	.000		
	tailed)	87	87	87		
	Ν					
Loan Portfolio	Pearson	.780*	.700	.502	1	
	Correlation					
	Sig. (2-	.000	.000	.000		
	tailed)	87	87	87	87	
	Ν					
Board Size	Pearson	.677*	.236	.562	.125	1
	Correlation					
	Sig. (2-	.000	.000	.000	.000	
	tailed)	87	87	87	87	87
	Ν					

Table 6: Correlation Matrix

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

The results of the Pearson correlation analysis demonstrate а relationship between firm characteristics and the financial performance of microfinance institutions (MFIs) in Eldoret City, Kenya. The analysis shows that all the independent variables—Firm Leverage, Firm Liquidity, Loan Portfolio Size, and Board Size-are positively and significantly correlated with financial performance at the 0.05 level of significance. Among these, Firm Liquidity shows the highest correlation with financial performance (r=0.856, p=0.000), indicating that higher levels of liquidity are linked to better financial results. This may be attributed to enhanced cash flow management and an increased capacity to fulfill financial commitments. Loan Portfolio Size also demonstrates a strong positive correlation (r=0.780, p=0.000), implying that MFIs with larger loan portfolios tend to experience

better financial performance, likely due to increased interest income and loan diversification. Firm Leverage (r=0.715, p=0.023) and Board Size (r=0.677, p=.000) also show positive associations with financial performance, indicating that effective debt management and governance structures contribute to financial success. Furthermore, intervariable correlations show that firm liquidity and Firm Leverage (r=0.711, p=0.000), as well as firm liquidity and Loan Portfolio Size (r=0.502, p=0.000), have strong positive relationships, highlighting the interconnected nature of financial characteristics in MFIs. These results reveal the importance of strategic financial management, loan portfolio expansion, and governance structures in enhancing the financial performance of MFIs in Eldoret City.

Linear Regression Analysis

Table 7 presents the outcomes of the linear regression analysis carried out to determine how firm characteristics influence the financial performance of MFIs operating within Eldoret City. The analysis yielded an R-value of 0.792, signifying a strong and positive correlation between the independent variables (firm characteristics) and the dependent variable (financial performance). Additionally, the R-squared statistic was reported at 0.627, implying that 62.7% of the variability in financial performance among these institutions can be accounted for by the combined effects of firm leverage, firm liquidity, loan portfolio, and board size. The remaining 37.3% of the variation may be due to other variables or external influences that were beyond the parameters of this particular study.

Furthermore, the ANOVA results revealed that the overall regression model was statistically significant. This was evidenced by a p-value of 0.000, which is well below the threshold of significance (p < 0.05). Such a result confirms that

the model provides a statistically significant prediction of financial performance, suggesting that firm characteristics collectively have a meaningful impact on the financial outcomes of MFIs in Eldoret City.

Examining the coefficients of the regression model, it emerged that firm leverage exerts a negative and statistically significant effect on financial performance, as indicated by a beta coefficient of -0.215 and a p-value of 0.002. In contrast, firm liquidity was found to have a positive and significant influence, with a beta coefficient of 0.342 and a highly significant p-value of 0.000. Among the predictors, the loan portfolio exhibited the strongest positive impact on financial performance, demonstrated by a beta value of 0.476 and a p-value of 0.000; this suggests that expanding the loan portfolio is associated with enhanced financial outcomes. Finally, board size also showed a positive and statistically significant relationship with financial performance, reflected in a beta coefficient of 0.198 and a p-value of 0.001.

Model Summary									
Model	R F	R Square Ac	ljusted R Squar	e Std. E	rror of the E	Estimate			
1	.792 ^ª	.627	.608		0.045				
a. Predictors: (Constant) Firm Leverage, Firm Liquidity, Loan Portfolio, Board Size									
b. Dependent Variable: Financial Performance									
			ANOVA						
Model		Sum of Squa	res df	Mean Square	F	Sig.			
1	Regression	3.450	4	0.862	22.15	.000 ^b			
	Residual	2.050	83	0.046					
	Total	5.500	87						

Model	Unstanda	rdized Coefficients	Standardized Coefficients	t	Sig.
	В	Std. Error	Beta		•
(Constant)	0.567	0.102		5.56	0.000
Firm Leverage	-0.215	0.064	-0.301	-3.36	0.002
Firm Liquidity	0.342	0.079	0.428	4.33	0.000
Loan Portfolio	0.476	0.085	0.521	5.60	0.000
Board Size	0.198	0.058	0.312	3.41	0.001

a. Dependent Variable: Financial Performance

Based on the findings of the study, the following is the resulting regression model:

Y = 0.567 + -0.215 (Firm Leverage) + 0.342 (Firm Liquidity) + 0.476 (Loan Portfolio) + 0.198 (Board Size)

This regression equation illustrates that for every additional unit increase in Firm Leverage, the Financial Performance of the institution is expected to decline by 0.215 units, holding all other factors constant. Conversely, an increase of one unit in Firm Liquidity is associated with a positive improvement in financial performance by 0.342 units. Furthermore, a one-unit rise in the Loan Portfolio is predicted to enhance financial performance by 0.476 units. Similarly, increasing the Board Size by a single unit contributes to an increase in financial performance by 0.198 units.

In summary, the analysis indicates that while higher firm leverage negatively impacts financial outcomes, greater liquidity, an expanded loan portfolio, and a larger board size each have a positive and significant contribution to the financial success of MFIs in Eldoret City.

Discussion

Firm Leverage and Financial Performance

The research findings indicated that the level of leverage employed by MFIs in Eldoret City plays a crucial role in influencing their financial performance. A significant proportion of the participants in the study expressed strong agreement with the notion that MFIs encounter considerable difficulties in meeting their debt obligations promptly. This inability to service outstanding loans within the required timelines was highlighted as a key factor undermining their liquidity position. Consequently, these financial strains not only hinder day-to-day operations but also threaten the broader financial stability and sustainability of these institutions over time. This finding reflects the study by Wambua and Mwangi (2020), which established that institutional size, measured by total assets, positively correlates with profitability, with larger institutions demonstrating

stronger financial performance. However, higher leverage ratios were found to negatively impact financial sustainability due to increased debt servicing costs, which reduce available capital for lending and investment in operational improvements. Excessive reliance on borrowed funds can strain cash flows, limit strategic flexibility, and increase the risk of default leading to a weakened financial performance. This finding accentuates the need for MFIs to maintain an optimal debt-equity ratio to enhance financial stability while ensuring sustainable growth (Niu, 2018).

The respondents also strongly agreed that the MFIs effectively manage debt repayment obligations without financial distress. This finding contrast with those of Muthoni and Njuguna (2021), whose study found that the rural and urban poor, the primary clients of MFIs, often face unstable incomes, making loan repayment difficult, which in turn affects debt repayment obligations. However, the ability of MFIs in Eldoret City to manage debt repayment effectively suggests that these institutions implemented have robust risk management strategies, such as strict credit assessment, flexible repayment structures, and proactive loan monitoring mechanisms. Akong'a. (2019) emphasises the importance of sound financial management practices in improving the sustainability of MFIs. Furthermore, the effective management of debt repayment obligations indicate that MFIs in Eldoret City have diversified their income streams and strengthened their liquidity positions, allowing them to cushion against potential defaults and financial shocks.

The findings also reflect the Trade-Off Theory by Kraus and Litzenberger (1973), which suggests that firms balance the benefits of debt financing (such as tax shields) against the costs of financial distress to optimize their capital structure. The respondents' agreement that high financial leverage has positively impacted MFIs profitability and growth supports the theory's argument that debt can enhance firm value by reducing taxable income, thereby improving profitability. However, the respondents' neutrality regarding easy access to debt financing implies that while MFIs recognize the advantages of leverage, they may face constraints in securing external funding due to lender requirements, interest rates, or perceived credit risks. This concept aligns with the principles of the Trade-Off Theory, which posits that organizations carefully balance the advantages of taking on debt with the possible drawbacks associated with financial distress. Rather than persistently increasing their levels of debt, firms strive to maintain a capital structure that achieves an optimal balance between the tax benefits gained from debt financing and the heightened risk of insolvency that excessive borrowing can bring. By deliberately weighing these competing factors, companies aim to operate within a range of leverage that maximizes firm value while minimizing financial vulnerability.

Firm Liquidity and Financial Performance

The findings revealed that firm liquidity significantly affects financial performance of MFIs. The respondents agreed that the MFIs' liquidity ratios (e.g., current ratio, quick ratio) indicate strong financial health. This echoes those of Smith and Williams (2021), who revealed that MFIs with higher liquidity ratios performed better in terms of ROA and ROE, as they could meet short-term obligations. Johnson and Douglas (2022) argue that adequate liquidity ensures that MFIs can efficiently manage cash flows, reduce financial distress, and capitalize on investment opportunities without relying on costly external financing. Furthermore, Muturi and Otieno (2023) state that strong liquidity improves operational resilience, allowing MFIs to navigate economic downturns, meet unexpected expenses, and sustain long-term growth. This reflects previous studies that emphasise the critical role of liquidity in promoting financial stability and investor confidence improving in financial institutions.

The respondents agreed that the MFIs regularly review and optimize their current assets to improve

liquidity. They also effectively manage their current liabilities to avoid liquidity risks, ensuring they maintain a stable financial position. This proactive liquidity management approach enables MFIs to meet their short-term obligations while sustaining operational efficiency. The finding aligns with Clark and Brown (2018), who found that MFIs routinely assess their liquidity ratios and adjust them in response to changes in the macroeconomic environment. Their study further emphasised that liquidity optimization is essential in mitigating financial distress, enhancing investor confidence, and ensuring continued access to credit markets. As argued by Tom (2015) MFIs can safeguard their financial sustainability, minimize the risk of cash flow disruptions, and improve their overall financial performance by maintaining a well-balanced liquidity strategy.

The findings are supported by the Liquidity Preference Theory, which asserts that firms and individuals prefer to hold liquid assets to meet short-term obligations, manage uncertainties, and take advantage of emerging opportunities. The respondents' agreement that MFIs have a wellstructured repayment schedule and maintain sufficient current assets to cover short-term obligations reflects the core principles of this theory. According to Keynes (1930), businesses prioritise liquidity to ensure financial stability and operational continuity, especially in unpredictable economic environments. For MFIs, maintaining adequate liquid assets ensures they can meet depositor withdrawals, honour short-term debt, and sustain lending activities without financial distress. Moreover, by strategically balancing liquid assets and obligations, MFIs can optimize financial performance while minimizing the risks associated with illiquidity. This justification reinforces the argument that effective liquidity management, guided by the preference for holding readily available cash or near-cash assets, is a fundamental determinant of financial sustainability and resilience in the microfinance sector.

Loan Portfolio and Financial Performance

The findings revealed that loan portfolio significantly affect financial performance of MFIs as the respondents strongly agreed that MFIs have a well-defined creditworthiness assessment framework to evaluate loan applicants. Furthermore, they have an efficient loan approval process that ensures the timely disbursement of funds, thereby enhancing operational efficiency and customer satisfaction. These findings align with those of Kivuva (2019), who found that loan portfolio size positively influences financial performance. However, this relationship is moderated by the quality of the loan portfolio and risk management practices. A well-managed loan portfolio not only drives profitability but also mitigates the risk of NPLs, ultimately strengthening the financial sustainability of MFIs (Mthethwa, 2019). Effective credit assessment and risk management strategies ensure that institutions extend credit to creditworthy borrowers, reducing default rates and improving loan portfolio health. Consequently, MFIs that adopt robust lending frameworks are better positioned to maximize returns on assets and equity while maintaining financial stability (Moyo & Sithole, 2021).

The majority of the respondents agreed that the use of advanced credit-scoring models has significantly improved loan portfolio quality, ensuring that loan approval decisions are based on clear, well-documented policies. This structured approach has enhanced risk management, reduced default rates, and contributed to overall financial stability among MFIs. A study by Moyo and Sithole (2021) corroborates these findings, revealing that MFIs with larger loan portfolios in South Africa exhibited higher profitability compared to their counterparts in Zimbabwe. This disparity was attributed to better economic conditions, more stable financial markets, and the adoption of robust credit assessment frameworks. Furthermore, operational efficiency emerged as a critical determinant of profitability in institutions managing extensive loan portfolios. Efficient credit risk

management, streamlined loan disbursement processes, and the integration of digital lending solutions have further strengthened the financial performance of MFIs.

The findings echoes the arguments in Modern Portfolio Theory (MPT), which emphasizes the importance of risk assessment and diversification in optimizing financial performance. MPT posits that investors or in this case, MFIs can achieve better financial outcomes by strategically managing risks associated with their portfolios. Regularly conducting portfolio risk assessments can help MFIs identify, evaluate, and mitigate potential risks, such as NPLs. The theory advocates for risk-return tradeoffs, where MFIs aim to maximize returns while minimizing exposure to high-risk loans (Markowitz, 1952). Through diversification of loan portfolios and thorough risk evaluation, MFIs can reduce default risks, ensuring a balanced and sustainable financial performance.

Board Size and Financial Performance

The findings revealed that board size significantly affects financial performance of MFIs, as the respondents also agreed that board diversity, including factors such as gender, expertise, and professional background, enhances financial performance. As explained by Andres and Vallelado (2018), diverse board brings a broader range of skills, experiences, and perspectives, which can improve decision-making, risk management, and strategic planning within MFIs. However, despite the perceived benefits of diversity, there remains an ongoing debate regarding the optimal board size for financial performance. This is echoed by Topal and Dogan (2014), whose study suggested that as the board size increases, coordination and decisionmaking efficiency may decline, leading to slower responses to market changes and diluted accountability. The negative relationship implies that an excessively large board can hinder agility and reduce financial performance, as reflected in declining ROA. These findings suggest that while enhances financial oversight diversity and governance, an optimal board size is crucial in

balancing effective management and financial performance within MFIs.

The respondents also strongly agreed that frequent board meetings enhance financial oversight and risk management in micro-finance institutions. They that also emphasized higher educational qualifications among board members contribute to informed financial decision-making, more ultimately improving institutional performance. This aligns with the findings of Lipton and Lorsch (2022), who argued that while board composition plays a crucial role in governance, excessively large boards tend to be ineffective due to issues such as loafing and free-riding among directors. In such scenarios, a lack of engagement and accountability can hinder the quality of strategic decision-making, leading to inefficiencies in financial oversight. Furthermore, research suggests that smaller, well-structured boards with highly qualified members are more agile and effective in responding to financial implementing risk challenges, management strategies, and fostering sustainable growth. Therefore, ensuring an optimal board size, coupled with frequent meetings and high educational qualifications, critical in strengthening is governance and enhancing financial performance in micro-finance institutions.

The relevance of contemporary frameworks such as the Agency Cost Theory cannot be overstated, particularly in understanding the dynamics between principals (shareholders or owners) and agents (managers). This theory suggests that inherent conflicts of interest often emerge between these two parties, giving rise to what are termed agency costs-expenses associated with monitoring, controlling, and aligning managerial actions with shareholder objectives (Panda & Leepsa, 2017). According to research findings, holding regular and frequent board meetings, coupled with having board members who possess substantial financial expertise, plays a pivotal role in minimizing agency while simultaneously enhancing costs an organization's financial outcomes. Regular board meetings create a platform for continuous oversight, facilitating strategic direction, increased accountability, and proactive intervention when necessary. This frequency helps curb managerial opportunism, ensuring that executives act in the best interests of the shareholders rather than pursuing personal gains. Moreover, the presence of board members with a strong background in finance adds considerable value to corporate governance processes. These financially literate directors contribute specialized insights into critical areas such as risk evaluation, financial strategy development, and adherence to regulatory frameworks. Their expertise strengthens the board's ability to oversee complex financial matters, which in turn leads to measurable improvements in key financial indicators, including return on assets, return on equity, and overall profitability. Therefore, when corporate governance mechanisms successfully align managerial incentives with shareholder goals, the organization's financial performance is likely to be positively influenced.

CONCLUSIONS AND RECOMMENDATIONS

Since firm leverage was found to have a statistically significant positive correlation with the financial performance of MFIs, this suggests that MFIs that strategically use leverage by acquiring debt to finance their operations tend to experience improved financial outcomes. The positive correlation suggests that borrowing enables these institutions to expand their loan portfolios, enhance revenue generation, and maintain operational efficiency. The ability of MFIs to manage their leverage effectively allows them to take advantage of financial opportunities, such as scaling up lending interest activities. increasing income. and strengthening their market position. However, it is critical that these institutions strike a balance in their debt financing strategies to avoid excessive borrowing, which could lead to financial distress and increased default risks.

The findings further indicate the existence of a statistically significant and positive relationship between liquidity and the financial performance of

MFIs. This outcome implies that institutions maintaining higher levels of liquid assets are more capable of fulfilling their short-term financial commitments, thereby enhancing their operational effectiveness. In addition, strong liquidity positions enable MFIs to capitalize on timely investment prospects that contribute to increased profitability. This underscores the critical role of maintaining sufficient liquidity reserves as a protective measure against financial volatility and unforeseen cash flow challenges. By ensuring the availability of adequate liquid resources, MFIs not only safeguard their operational continuity but also strengthen their capacity to provide uninterrupted credit services to their clientele. Moreover, healthy liquidity levels bolster the overall financial resilience of these institutions, minimizing their vulnerability to financial distress that could result from unexpected shortfalls in cash inflows. Therefore, it is imperative that liquidity management be prioritized as a central component of strategic planning for MFIs that aim to enhance their financial sustainability, achieve long-term growth, and maintain a competitive edge within the financial services sector.

The findings further indicate the existence of a statistically significant and positive relationship between loan portfolio and the financial performance of MFIs. This suggests that as MFIs expand their loan portfolios, their financial performance improves, likely due to increased interest income and enhanced financial sustainability. A well-diversified loan portfolio enables MFIs to reach a broader customer base, spreading credit risk while maximizing revenue generation. Moreover, an efficiently managed loan portfolio ensures timely repayments, reducing default rates and enhancing overall institutional stability. These results align with previous studies indicating that MFIs with larger and well-structured loan portfolios experience better financial health and resilience against economic fluctuations. Consequently, microfinance institutions should adopt strategic loan portfolio management

practices, such as risk assessment, credit scoring, and portfolio diversification, to optimize financial outcomes.

The findings further indicate the existence of a statistically significant and positive relationship with financial performance of MFIs. This suggests that larger boards contribute positively to financial outcomes, likely due to the diversity of expertise, broader oversight, and improved governance mechanisms they provide. A well-structured board ensures better decision-making, strategic guidance, and risk management, which are critical for the sustainability and profitability of MFIs. Moreover, a larger board offers increased networking opportunities, which can enhance access to funding, regulatory compliance, and institutional credibility. These factors collectively strengthen financial performance by ensuring accountability, operational efficiency, and better resource allocation.

Based on the conclusion that firm leverage has a statistically significant positive correlation with the financial performance, the study recommends the importance of а well-structured financial management framework to ensure that the benefits of leveraging are maximized while minimizing associated risks. Regulatory compliance and prudent debt management practices should be emphasized to ensure sustainable financial growth for MFIs. Policymakers and financial regulators should consider measures that enhance access to affordable credit while promoting responsible borrowing practices among microfinance institutions. Furthermore, MFIs should continuously assess their leverage ratios to maintain optimal capital structures that support long-term profitability. These findings contribute to the broader discourse on financial performance in the microfinance sector, underscoring the need for strategic debt utilization as a tool for enhancing institutional growth and stability.

The positive correlation between liquidity and financial performance calls for prudent financial management policies that balance liquidity with profitability in MFIs. While excessive liquidity may indicate inefficiencies in asset utilization, a wellmanaged liquidity position enables MFIs to respond effectively to borrower demands, mitigate credit risks, and optimize interest income. The findings imply that regulatory bodies and policymakers should encourage MFIs to adopt robust liquidity management frameworks, ensuring that they maintain optimal liquidity levels without compromising lending activities. Furthermore, MFIs should explore innovative financial solutions such as digital banking and diversified revenue streams to enhance liquidity and financial resilience. It is advisable for MFIs in Eldoret City to strengthen their liquidity management practices so that they can achieve long-term growth and continue providing essential financial services to underserved communities.

Furthermore, the positive correlation between loan portfolio size and financial performance demonstrates the critical role of credit expansion in promoting financial inclusion and economic empowerment within Eldoret City. MFIs can enhance their competitiveness while fulfilling their core mandate of providing accessible financial services by offering diverse loan products tailored different customer segments. However, to institutions must balance portfolio growth with effective risk management frameworks to mitigate potential credit risks that could arise from overlending or economic downturns. Policymakers and financial regulators should support MFIs by providing an enabling environment that promotes responsible lending practices, effective credit risk management, and regulatory compliance. These findings reinforce the importance of loan portfolio management as a key determinant of financial

performance, demonstrating the need for MFIs to adopt data-driven lending strategies and financial innovations to sustain long-term profitability.

However, while a larger board size presents benefits, it is crucial for MFIs to maintain an optimal balance to avoid potential drawbacks such as decision-making inefficiencies and bureaucratic complexities. The findings suggest that board composition, experience, and independence also play a vital role in enhancing financial performance, beyond just the number of board members. Therefore, microfinance policymakers and institution managers should focus on appointing qualified and experienced board members who can contribute to strategic financial planning and risk management. Future research could explore the ideal board size that maximizes financial performance while minimizing governance challenges in microfinance institutions.

Suggestions for Further Research

Future research could explore other firm characteristics besides the ones this study focused onto provide a broader understanding of the financial performance of MFIs. For instance, examining the role of firm age, ownership structure, or managerial expertise could offer unexplored factors affecting financial sustainability. Furthermore, comparative studies across different cities or counties in Kenya could help determine whether regional economic factors influence the relationship between firm characteristics and financial performance. Also, incorporating qualitative approaches, such as case studies or interviews with industry experts, could enhance understanding of contextual challenges faced by MFIs.

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