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Abstract

Purpose: This study delineates the impact of development banking on Kenya's economic growth. The current study adopted a quantitative and exploratory research design.

Materials and Methods: The study used a quantitative research design. Secondary data was utilized in this study. The data was collected from the financial statements of development banks in Kenya. The target population was 6 development banks in Kenya. The study then progressed to more complex regression analysis, where financial performance ratios and percentages for predictor factors formed the basis of the analysis. The study focused on 6 development financial institutions operating in Kenya.

Findings: The findings ($\beta=0.1153$, $p=0.0056$), reveal that development banking had a positive and significant effect on economic growth. This infers that an improvement in development banking by one unit would lead to an improvement in economic growth by 0.115 units. The

investigation substantiates a tangible and statistically significant correlation between the maturation of the development banking sector and the economic growth spectrum in Kenya.

Implications to Theory, Practice and Policy: Policymakers in Kenya should work to maintain a stable regulatory system that enhances the role of the banking system in stimulating economic growth. The study emphasizes the need for a stable regulatory environment and well-considered interest rate policies to mitigate adverse economic impacts. Additionally, the study advocates for a pro-poor banking approach to reduce wealth disparities and boost economic growth through improved savings and customer deposits in banks.

Keywords: *Development Banking, Economic Growth, Foreign-Owned Banks, Financial Sector Development, Patient Capital, Financial Intermediation, Financial Inclusion, Financial Sector Reforms, Regression Analysis*

1.0 INTRODUCTION

Economic expansion is crucial, especially in emerging markets, as it plays a key role in elevating living conditions, diminishing poverty, and generating job opportunities, which, in turn, boost income levels. This growth is driven by the output of goods and services across different sectors of the economy, contributing significantly to overall societal prosperity (Joseph, 2020). According to Sindani and Buchichi (2013), financial institutions play a crucial role in the economic development of any country. They argue that the sophistication and effectiveness of the financial sector are directly correlated with improved economic performance, higher levels of investment, and general growth.

Financial institutions are pivotal in an economy by effectively mobilizing and pooling domestic savings and channeling them into productive capital investments. This process not only fosters economic growth but also encourages innovation and structural change. As such, a competitive and well-developed financial sector is an important contributor to economic growth. For the banks to achieve the role of economic growth, they need to encourage and mobilize savings, intermediate these savings at low cost, ensure savings are channeled into efficient investment (including in innovation and structural change) as well as help manage the risks for individuals and enterprises. In the context of industrial policy, it should help to fund new sectors deepen existing ones, and support national and regional development strategies. Ideally, the financial sector could help societies acquire and accumulate learning, valuable for increasing productivity, especially in a dynamic sense (Stiglitz and Greenwald 2013).

Bongini et al. (2017) indicated that the role that financial institutions play in fostering economic growth can be divided into two; (i) an important source of innovation, competition, and efficiency, with positive spill-over effects for the functioning of the banking system of the host country; or (ii) a source of credit contraction in the credit markets of host countries, for a variety of reasons, among which exposure to the financial troubles, either firm-specific or systematic, of their parent company is at present the most significant.

In this dynamic financial ecosystem, development banks emerge as unique entities, distinctively positioned to invigorate economic growth, particularly in sectors often overlooked by traditional commercial financial institutions. Their fundamental role lies in providing 'patient capital', which typically involves financing at comparatively lower interest rates and a readiness to assume greater risks. This approach is especially crucial for startups and ventures in less attractive investment domains, which might otherwise struggle to secure funding. Development banks are thus not merely financiers but catalysts, spurring investments in sectors deemed too risky or unprofitable by conventional banking standards (Kleiterp, 2017). By offering more flexible and long-term financial solutions, these institutions play a pivotal role in bridging the investment gap in critical yet underfunded sectors (Clark & Sunderland, 2018). This strategic financing approach is instrumental in fostering innovation, encouraging sustainable practices, and driving economic development in both emerging and established markets. Their operations, therefore, extend beyond mere financial transactions, contributing significantly to socio-economic development and the broader realization of national and regional development objectives.

Gottschalk et al. (2016) discuss the role of development banks in providing finance for long-term, capital-intensive investments. These banks uniquely blend lending with equity participation, enabling them to closely monitor and influence projects. Their approach goes beyond mere

financing, involving active engagement in project governance and decision-making on technology, scale, and location. This not only exemplifies their hands-on strategy but also underscores their commitment to ensuring the success of the ventures they back.

Development banks extend their influence by underwriting equity securities, showcasing their capacity to leverage resources. This role is pivotal in attracting additional lenders, especially those lacking the expertise to evaluate a project's feasibility and potential. By offering guarantees, they further bolster investor confidence. Moreover, development banks play a critical countercyclical role, sustaining investment during economic downturns and thus safeguarding a country's productive structure, as detailed by Gottschalk, Poon, & Mednik (2016).

In Kenya, development banking plays a critical role in the nation's economic landscape, primarily by providing financial support to sectors that are pivotal for growth yet underserved by conventional commercial banks. These institutions focus on long-term investments in key areas such as infrastructure, agriculture, and small to medium enterprises, offering more favorable terms and lower interest rates to facilitate sustainable development. Their strategic investments not only drive economic expansion but also contribute significantly to job creation and poverty reduction. Furthermore, Kenyan development banks are instrumental in implementing government economic policies and initiatives, particularly those aimed at achieving the goals outlined in Kenya's Vision 2030.

Problem Statement

The economic landscape of Kenya, marked by its fluctuating growth rates since 1961, presents a compelling case for examining the role of development banking in stimulating economic growth. Despite a notable high of 22.174% GDP growth in 1971, there has been a consistent decline, with rates dropping to 4.804% in 2017, and further from 5.869% in 2016 to 4.874% in 2017, as reported by the World Bank (2018). This downward trajectory continued with a decrease from 6.318% in 2018 to 5.366% in 2019 (Kimani & Maingi, 2021). The latest figures in 2022 show a growth rate of below 5% with projections for 2024 being slightly above 5%. This trend underscores the urgency for an in-depth understanding of the factors influencing Kenya's economic performance, particularly the role of the development banking sector, which Oketch (2020) identifies as crucial in achieving the objectives of Vision 2030 through effective financial intermediation.

While studies in other regions, such as Almahadin et al. (2021) in Jordan, have explored the impact of banking industry development on economic growth, there is a noticeable gap in context-specific research for Kenya. Similarly, research focusing on specific banking models, like Islamic banking by Walid (2015), and the role of commercial banks as studied by Mohamed (2020), indicate a conceptual and methodological gap in understanding the broader spectrum of banking influences, including development banking, on Kenya's economic growth. This gap points to a critical need for comprehensive research that specifically investigates the role of development banking, encompassing both conventional and non-conventional banks, in driving economic growth in Kenya. Therefore, this study aims to fill this gap by exploring the relationship between development banking and economic growth in Kenya, offering insights into long-term strategic development and policy implementation

Objectives of the Study

To determine the role of development banking in economic growth in Kenya

Research Questions of the Study

What is the role of development banking in economic growth in Kenya?

Significance of the Study

This study holds substantial significance for a wide range of stakeholders in Kenya's financial sector, particularly at a time when rapid advancements in banking technology are poised to reshape the industry's landscape. By expounding the relationship between the evolution of the banking sector and national economic growth, this research offers insights to banking executives and policy makers. These insights will enable them to strategize effectively, fostering robust and positive economic development. Crucially, the findings of this study are poised to serve as a vital resource for other key policymakers. As these entities strive to fulfill ambitious economic development goals, particularly those enshrined in Kenya's Vision 2030, this research will be instrumental. It provides a detailed understanding of how the banking sector can act as a catalyst for double-digit economic growth, thereby helping in the formulation of macroeconomic and fiscal policies that strengthen financial sector stability and spur economic advancement.

Moreover, this study contributes significantly to the academic sphere by expanding the existing body of literature on development banking and its impact on economic growth in Kenya. The insights gained will not only enrich current academic discourse but also pave the way for future research. Scholars and academicians can utilize these findings to delve deeper into the role of development banking in economic contexts similar to Kenya's, fostering a richer understanding and facilitating informed policy interventions. In essence, this study is not just a reflection of current economic dynamics but a beacon guiding future explorations and policy formulations in the realm of development banking and economic growth.

2.0 LITERATURE REVIEW

Theoretical Review

The Modern Economics Theory

The first theoretical underpinnings of this study are anchored in the Modern Economics Theory, primarily influenced by the pioneering works of Solow (1956) and Swan (1956). This theory postulates that the utility of capital incrementally decreases, implying that simply increasing capital investment results in diminishing returns and therefore has a limited and transient effect on amplifying economic growth. A key insight from this model is the realization that sustainable economic growth is not solely contingent on capital accumulation but is critically dependent on the enhancement of technology and labor productivity.

Recent economic scholarship has further expanded on this theory, elucidating how myriad decisions and anticipations by individuals contribute to emergent societal attributes. These include variables such as national income levels, inflation rates, productivity gains, cultural values, and the valuation of various social norms and forms of capital. Sohail and Shanmugham (2003) highlight a dual challenge in economic theory: the impact of individual decisions on emergent societal features and the influence of fast-moving policy variables on these features. They note that while emergent properties like culture, institutional arrangements, and attitudes are recognized, they are often inadequately incorporated into economic models.

Tiwari, Herstatt, and Buse (2006) further develop this idea by illustrating that financial returns in rapidly changing environments are contingent upon subtle and often overlooked shifts in these slower-moving societal structures. These shifts can precipitate unexpected crises, suggesting a complex interplay between fast and slow-moving economic features. The relevance of Modern Economics Theory to this study lies in its acknowledgment of a symbiotic relationship between financial development and economic growth. It proposes an alternate viewpoint where banking aspects, specifically technological advancements and capital allocation, are pivotal drivers of economic growth. This theoretical perspective is crucial for understanding the nuanced dynamics between development banking and economic growth, especially in the context of a rapidly evolving financial sector like Kenya's. It provides a sophisticated framework for analyzing how development banking, through its unique mechanisms of capital distribution and technological integration, can significantly contribute to sustainable economic growth.

The Bi-Directional Theory

The Bi-directional Theory, a paradigm shift in economic thought, was introduced by Jovanovic and Greenwood (1990) and subsequently supported by scholars such as Saint Paul (1992), Berthelemy and Varoudakis (1996), and Harrison, Sussman, and Zeira (1999). This theoretical model proposes a reciprocal relationship between financial development and economic growth, hence its designation as the 'Bi-directional' or 'Feedback' hypothesis. It posits that not only does financial development stimulate economic growth, but economic growth, in turn, catalyzes the evolution of the financial sector.

This interdependence is further expounded by Schumpeter (1934), who argued that a robust financial system could spur economic growth through technological innovation and the development of new products and services. This, in turn, necessitates adaptations by banking institutions to these innovations, thereby fostering enhanced economic performance. For instance, the emergence of mobile banking in companies like Safaricom exemplifies this dynamic interaction. Empirical support for this theory is widespread. Shan, Morris, and Sun (2001) examined 30 developing countries and concluded that the relationship between financial and economic development is mutually causal. This view is corroborated by studies such as Wood (1993) and Chuah and Thai (2004). Notably, Akinboade (1998) identified a bi-directional causality between per capita income and financial development in Botswana between 1972 and 1995, suggesting that economic growth and financial development are complementary processes.

Jung (1986) conducted a comprehensive study involving 56 countries, concluding that the causality from financial growth to economic development is more prevalent than the reverse, particularly in developing countries. In contrast, developed countries often exhibit the opposite trend. Hussein and Demetriades (1996), despite their limited sample of 16 countries, also observed that the relationship between financial development and economic growth varies across different nations, thereby challenging any notion of a universal trend in financial-economic causality.

The Bi-directional Theory is pivotal to this study as it aligns with the observed correlation between the development of the financial sector and economic growth in various countries. This hypothesis harmoniously agrees with a correlation between the development of finance and the growth of the economy in any country.

Empirical Studies

Global Perspective

Yemelyanova (2021) delved into the synergy between stock market and banking sector developments and their collective impact on economic growth in Central and Eastern European (CEE) countries. Utilizing Granger causality tests and linear regression models, the study underscores the pivotal role of stock market development in attracting foreign direct investment and spurring economic growth. It reveals how stock market capitalization indirectly influences economic growth by impacting banking sector dynamics and gross capital formation. This research is particularly notable for its period of study, 1999-2015, during which it identifies both positive impacts of stock market size and negative implications of domestic credit to the private sector on economic growth. The study's call for enhanced stock market development in CEE countries to boost economic growth underlines its practical implications, though it left a contextual gap for exploration in the Kenyan setting.

Daly and Frikha (2016) examined the impact of Islamic finance on economic growth in developing countries. By comparing Islamic banks (IBs) with conventional banks using data from 120 banks between 2005 and 2012, the study reveals that non-usurious banking models significantly contribute to economic growth. It also highlights the synergistic effect of combining Islamic and conventional banking practices on economic growth, thereby suggesting an understanding of financial sector development. However, the study did not address the specific role of development banking, presenting an area for further inquiry.

Bongini et al. (2017) investigated the role of financial development, particularly the influence of foreign-owned banks, on the economic growth of Central, Eastern, and South-Eastern European countries in the post-communist era. This period, marked by the opening of financial markets and the global financial crisis, offers a unique context for understanding the dynamics of financial development. The study challenged conventional notions by questioning the universally positive impact of bank credit and foreign-owned banks on economic growth, thereby offering a critical perspective on the banking sector's contribution to economic growth in these regions.

Almahadin et al. (2021) focused on Jordan, examining the impact of banking industry development on economic growth through time-series econometric methodologies. The study's findings align with the supply-leading hypothesis, confirming the vital role of banking development in stimulating economic growth. However, it also highlighted the adverse effects of rising lending interest rates on economic growth, thereby providing a comprehensive view of the banking industry's influence in Jordan.

Regional Studies

El Menyari (2019) explored the impact of financial development and foreign banks in Africa, particularly in North and Southern Africa, from 1995 to 2015. The study, employing a system GMM estimator, found a positive correlation between the entry of foreign banks and economic growth in these regions. Conversely, in West, Central, and East Africa, this correlation was either negative or insignificant. This study underscores the varying influence of foreign banks across different African regions and calls for policies that bolster the financial sector to meet the continent's diverse needs. The study focused on Africa while the current study will be done in Kenya.

Apere (2016) focused on the impact of microfinance banks on economic growth in Nigeria. This study made use of quantitative secondary data from the Central Bank of Nigeria (CBN) statistical bulletin (2013) to carry out this study. The empirical perspective of this study employed the Augmented Dickey-Fuller Unit Root Test, cointegration test, error correction model (ECM) and the parsimonious test. Empirical evidence from the study has shown that the activities of microfinance bank can influence the entire economy if it is well coordinated. The results of the study indicate that microfinance bank loans and domestic investment significantly and positively affect the growth of Nigeria's economy based on the magnitude and the level of significance of the coefficient and p-value and, there is a long-run relationship between microfinance bank loans, investment and economic growth in Nigeria. The study however left out the aspect of development banking thus showing a conceptual gap.

Abubakar and Gani (2013) reevaluated the link between banking sector development and economic growth in Nigeria from 1970 to 2010. They found that liquid liabilities of commercial banks and trade openness positively influenced economic growth, while credit to the private sector, interest rate spread, and government expenditure had a negative impact. This study suggests the need for financial reforms focusing on diversifying financial instruments and reducing government borrowing. The policy implications are these; financial reforms in Nigeria should focus more on deepening the sector in terms of financial instruments so that firms can have alternatives to banks' credit which proved to be inefficient and detrimental to growth, moreover, government should inculcate fiscal discipline to reduce excessive borrowing from the financial sector and thereby crowding out private investment. The study was done in Nigeria while the current study will be done in Kenya.

Joseph (2020) investigated the causal relationship between bank credit and economic growth in Tanzania. Utilizing time series data from 1993-2017. Causality test and vector error correction were applied. Results from the study found no short-term causal relationship between bank credit and economic growth. In the long run, bank credit has a significant positive effect on economic growth. Policies towards enhancing the growth of financial sector should be emphasized to enable an increase in credit provision and promote economic growth through investment in different sectors of the economy. The positive long-run effect of financial intermediation means that enhancing deposit mobilization still remain paramount towards credit provision by banking financial institutions. The study however left out the aspect of development banking.

Mekango (2021) focused on the Ethiopian banking sector's development and its effect on economic growth to investigate the effect of banking development on economic growth for Ethiopia. Using an Autoregressive Distributed Lag model, the study found that indicators such as bank credit to the private sector positively influenced economic growth. However, when banking sector development indicators entered the model individually, only PSC is found to have positively and significantly determined economic growth after its first lag. Overall, although the effect is dependent on the banking indicator used, the evidence suggests that banking sector development is contributing positively to Ethiopian economic growth and. Hence, policies to encourage further development in the banking sector is useful in improving the Ethiopian economy. The study was done in Ethiopia context while the current study was done in Kenya.

Lupai Moses (2013) studied the impact of foreign banking institutions on economic growth in South Sudan to find out if there is any relationship between Foreign Banking Institutions and the level of Economic Growth in South Sudan. The study established that there was a very slow level

of economic growth as well as no relationship between foreign banking institutions and economic growth in South Sudan. The researcher concluded that Foreign Banking institutions do not contribute positively towards economic growth and recommended the government of South Sudan through the central bank and the national legislative assembly to review monetary policy to regulate the operations of those banks.

Kenyan Perspective

Ruibi (2012) conducted an extensive study on the influence of investment banking on Kenya's economic growth. Utilizing a comprehensive dataset from the Nairobi Securities Exchange (NSE), the study highlighted the critical role of investment banks in enhancing capital bases, minimizing operational costs, and diversifying revenue strategies. It was observed that investment banks play a pivotal role in maintaining a balanced portfolio of liquid assets and reducing non-performing loans, thereby contributing to the stability and growth of the Kenyan economy. However, the study did not explicitly address the role of development banking, indicating a gap in the research landscape.

Nyasha and Odhiambo (2017) explored the correlation between banking and stock market development and economic growth in Kenya. Their empirical analysis, utilizing a means-removed average methodology, revealed that while market-based financial development positively impacts economic growth, bank-based development does not exhibit a significant effect. This finding is critical as it challenges the conventional wisdom regarding the role of traditional banking in economic development, yet it overlooks the specific contribution of development banking.

Walid (2015) focused on the role of Islamic banking in economic growth in Kenya. The study adopted a quantitative research design. The population of interest comprised two fully-fledged Islamic banks in Kenya and four other banks that offer Islamic banking services in Kenya. The study utilized secondary data from the financial statements of the Islamic for a period of six years from 2008-2014. The data collected was analyzed using the Karl Pearson correlation and multiple linear regression using the statistical package for social studies. The study findings established that the level of total savings had a positive relationship with economic growth while total advances had a negative relationship with economic growth. The study concludes that an increase in savings in Islamic banks stirs economic growth while a decrease in lending inversely affects economic growth while an increase in lending by Islamic banks stirs economic growth.

Randiki (2016) investigated the relationship between banking sector development and economic growth in Kenya, revealing only a weak correlation between these two variables. The study analyzed the data using SPSS version 20. In this study, various sector actors like financial assets indicate that a minimal positive statistically estimated relationship exists with economic growth, again at the correlation of coefficient, the study explains that every 2.438 million Kenya shillings invested in banking sector assets propels the economic growth by 1 million Kenya shillings. The minimal relationship was also evidenced by deposits and liquid liabilities at weak negative correlations. The study was descriptive in nature thus showing a methodological gap. The current study adopted a desktop research design.

Mohamed (2020) focused on the role of commercial banks in Kenya's economic development, revealing a strong correlation between both short and long-term loans and economic growth. Findings from the regression analysis determined that the coefficient of correlation shows that there was a strong linear relationship between long- and Short-term loans, account deposits, and

economic development. The ANOVA revealed that the model was statistically fit and thus it would be accurate to predict economic development based on short-term loans, long-term loans, and account deposits. Findings from the coefficients table showed that each variable had a different strength in predicting economic development. Short-term loans and account deposits were positive predictors of economic development while long-term loans were a negative predictor of economic development. It was established that for every unit increase in short-term loans, economic development went up

Research Gaps

Yemelyanova (2021) delved into the synergy between stock market and banking sector developments and their collective impact on economic growth in Central and Eastern European (CEE) countries. The study's call for enhanced stock market development in CEE countries to boost economic growth underlines its practical implications, though it left a contextual gap for exploration in the Kenyan setting. Daly and Frikha (2016) study did not address the specific role of development banking, presenting an area for further inquiry. Joseph (2020) investigated the causal relationship between bank credit and economic growth in Tanzania. The study however left out the aspect of development banking.

Almahadin et al. (2021) study was done in Jordan thus showing a contextual gap. The current study was done in Kenya. El Menyari (2019) study was done in North and Southern Africa. Apere (2016) however left out the aspect of development banking thus showing a conceptual gap. Mekango (2021) study was done in Ethiopia context while the current study was done in Kenya. Randiki (2016) study adopted a desktop research design nature thus showing a methodological gap. The current study adopted a quantitative research design.

Conceptual Framework

The contextual framework presents the connections among variables.

Independent Variables

Financial Leverage



Dependent Variable

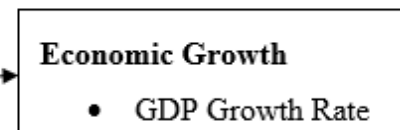


Figure 1: Conceptual Framework

3.0 METHODOLOGY

Research Design

Research design is the strategy or plan, that is used to obtain respondents, and how to collect data from them, to arrive at conclusions about a research question (Akhtar, 2016). There are three basic types of research design: qualitative research design, quantitative research design and mixed-method research design. The study adopts a quantitative research design, specifically an explanatory approach as defined by Akhtar (2016) and further elaborated by Etikan & Bala (2017). This design was adopted for its efficacy in explaining the cause-and-effect relationships among

various factors. It enables a systematic exploration of how specific aspects of development banking influence economic growth, thereby offering clarity and precision in understanding these complex dynamics (Etikan & Bala, 2017).

Data Collection

Cote (2021) defines data collection as the methodological process of gathering information about a specific subject. It is a systematic and standardized process of gathering and measuring information on variables that are relevant to a specific research topic or purpose. There are two types of data; primary and secondary data. Secondary data was utilized in this study. The data was collected from the financial statements of development banks in Kenya. The target population was 6 development banks in Kenya.

Data Analysis

To analyze the collected data, both descriptive and inferential statistical techniques were utilized. Descriptive statistics such as standard deviation, minimum, maximum, and mean were employed to present an initial understanding of the data patterns. The study then progressed to more complex regression analysis, where financial performance ratios and percentages for predictor factors formed the basis of the analysis.

Independent variables (development bank) and one dependent variable (Y), a proxy for economic growth, make up the multiple regression model used in this study.

The multiple regression model applied in the study was formulated as follows:

$$Y_{it} = \alpha + \beta_1 X_{1it} + \gamma Z_{it} + \varepsilon$$

where;

Y_{it} represents the dependent variable, Economic growth (measured by GDP growth rate),

X_{1it} denotes the independent variable, development banking (specifically focusing on long-term loans),

γZ_{it} represents control variables that might influence economic growth, like inflation rate, unemployment rate, or technological advancements, with γ as their coefficient.

ε is the error term.

This model was carefully constructed to isolate and examine the impact of development banking on economic growth, controlling for other potential variables.

4.0 FINDINGS

Descriptive statistics

Descriptive analysis is one of the critical phases of statistical data analysis. It provides a clear conclusion on the distribution of data which helps in detecting errors and outliers. The study used the four common measures of descriptive statistics; minimum, maximum, mean, and standard deviation to present the data patterns.

Table 1: Descriptive Statistics

	Obs	Mean	Std.Dev	Min	Max
GDP growth rate	30	4.54	2.64022	-0.3	7.5
Long term loan	30	4520.01	1629.25	1269	6928

The results indicated that the minimum GDP growth rate was -0.30 and the maximum was 7.5. This indicates that the GDP growth rate ranged from -0.3% to 7.5%. On average the GDP growth rate was 4.54 between 2018 and 2022. The standard deviation was low at 2.64022 indicating that there was a high variation GDP growth rate from the mean. This infers that the GDP in Kenya has been fluctuating between 2018 to 2022.

Inferential Analysis

Inferential statistics helped in measuring the relationship among variables this included correlation analysis and regression analysis (Kothari, 2004). The inferential analysis was undertaken after subjecting the data to various tests. Therefore, this section contained the correlation and the regression results.

Correlation Analysis

Correlation is usually used to test the relationship between the dependent and the independent variable. Correlation results are presented in Table 2.

Table 2: Correlation Analysis

		GDP growth rate	Development banking
GDP growth rate		1	
Development	r	0.4945	1
	p	0.0055	

The correlation results showed that development banking had a positive and significant correlation with economic growth ($r=0.4945$, $p=0.0055$). This implies that an improvement in development banking would lead to a weak positive correlation with economic growth. The study findings agreed with Abubakar and Gani (2013) who found that development banking had a significant positive influence on economic growth

Regression Results

Regression analysis helps to establish the relationship between the variables by presenting the coefficients and P - values. Results are presented in Table 3.

Table 3: Regression Model

Economic growth	coef	Std.Err	t	P> t	Conf.interval
Development Banking	.029406	.0732104	0.40	0.0056	-1787196 .1199076
_cons	0.25511	1.47282	0.17	0.864	-2.7917 0.00456
F(1,23)=19.36					
Rsquare=0.4496					
p=0.0056					

The results showed that development banking accounts for 0.4496 of the variances in economic growth. This indicates that development banking was responsible for 44.96% of the differences in economic growth. Outcomes ($\beta=0.1153$, $p=0.0056$), were clear that development banking had a positive and significant effect on economic growth. This infers that an improvement in development banking by one unit would lead to an improvement in economic growth by 0.115 units. The study findings agreed with El Menyari (2019) whose findings indicated that foreign bank entry has a positive and significant impact on economic growth in the countries of North and Southern Africa

5.0 CONCLUSIONS AND RECOMMENDATIONS

Conclusion

This study examined on the role of development banking in economic growth in Kenya. The findings conclusively demonstrated that development banking plays a pivotal and significant role in enhancing the country's economic development, especially through patient capital. The positive impact of development banking on Kenya's economic growth is not only substantial but also instrumental in accelerating the nation's economic trajectory. This emphasizes development banking as a critical and indispensable catalyst for Kenya's economic prosperity.

Furthermore, the study shed light on the influential role of foreign-owned banks within the Kenyan economy. These banks have emerged as key players in driving innovation and introducing advanced banking practices. Their presence in the Kenyan market has had notable positive spillover effects, contributing significantly to the dynamism and competitiveness of the local banking sector. This, in turn, has positively influenced the overall economic growth of the country.

The findings of this study provide compelling evidence for policymakers and financial sector stakeholders to continue fostering an environment that supports and enhances the capabilities of development banks. This approach is essential not only for sustaining economic growth but also for achieving the broader developmental objectives outlined in Kenya's Vision 2030. The insights gained from this study offer a valuable blueprint for leveraging the potential of development banking to create a more inclusive, robust, and sustainable economic future for Kenya.

Recommendations

In the wake of this study's findings, it is paramount to underscore the vital role of development banking as a key driver of economic growth in Kenya. To optimize its impact, a strategic emphasis on expanding and diversifying the services offered by development banks is essential. This expansion should specifically cater to the unique financial needs of entrepreneurs and small businesses, often overlooked by traditional banking models. Tailoring services to these segments will significantly boost economic inclusivity and innovation.

Simultaneously, enhancing regulatory frameworks tailored to development banking is crucial. Such frameworks should foster an environment conducive to effective and innovative operations of development banks. This includes regulatory flexibility to encourage funding in novel or underfunded sectors, which are crucial for stimulating economic growth. In alignment with the Vision 2030 blueprint, development banks should also intensify their focus on pro-poor banking strategies. These strategies are vital in bridging the economic divide, ensuring that financial services are accessible across all societal levels, thereby facilitating equitable growth.

A key side of this strategy involves implementing favorable interest rate policies. These policies should be designed to support the growth-oriented agenda of development banks, with lower and stable interest rates to encourage investments in key economic sectors. Moreover, fostering public-private partnerships is another avenue through which development banking can be reinforced. Such collaborations between development banks and the private sector can lead to innovative financing solutions, unlocking new investment opportunities in critical areas of the economy.

Additionally, investing in capacity building and technological advancement within development banks is crucial for enhancing their operational efficiency and market responsiveness. This investment will enable development banks to become more impactful in their role as catalysts of economic growth.

By concentrating efforts on these strategic areas, development banking can be effectively harnessed as a pivotal tool in Kenya's quest for economic development. This approach will align with the goals of Vision 2030, ensuring a more inclusive and prosperous future for the nation, and solidifying the role of development banks as cornerstones of Kenya's economic landscape.

Areas of Future Research

For researchers interested in investigating this scope further, we propose several recommendations. To start with, they could go further by introducing interaction terms to explore the combined effects of different independent variables on economic growth. This can be particularly insightful in understanding how the impact of development banking (long-term loans) on economic growth might change under different conditions (*e.g., varying levels of inflation or technological advancements*). With this, they could consider extending the equation to

$$Y_{it} = \alpha + \beta_1 X_{1it} + \gamma Z_{it} + \delta(X_{1it} \times Z_{it}) + \epsilon$$

In this equation, $\delta(X_{1it} \times Z_{it})$ represents the interaction terms, where δ is the coefficient estimating the impact of the interaction between development banking and the control variables on economic growth.

Secondly, a researcher would wish to consider the fact that economic phenomena often exhibit non-linear relationships that linear models might not adequately capture. Introducing polynomial terms or employing non-linear regression techniques can provide a more defined understanding of the data. For instance:

$$Y_{it} = \alpha + \beta_1 X_{1it} + \beta_2 X_{1it}^2 + \gamma Z_{it} + \epsilon$$

Here, $\beta_2 X_{1it}^2$ represents a quadratic term for development banking, allowing the model to capture potential non-linear effects of development banking on economic growth.

Future researchers could also consider Structural Equation Modeling (SEM) which combines multiple regression analysis, factor analysis, and path analysis and allows for the examination of complex relationships between observed and latent variables. This would be particularly useful in disentangling the direct and indirect effects of development banking on economic growth, accounting for the mediating role of other variables.

Finally, potential researchers would consider Panel Data Analysis since given the longitudinal nature of economic data (*across time and potentially across different countries or regions*), employing panel data analysis techniques such as Fixed Effects or Random Effects models can

provide more robust insights. These models can control for unobserved heterogeneity that might bias the estimates in standard regression models.

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