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# What Drives Financial Innovations in Kenya's Commercial Banks? An Empirical Study on Firm and Macro-Level Drivers of Branchless Banking

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## ABSTRACT

This paper examines the firm- and macro-level drivers of financial innovations in Kenya's commercial banks. We focus on branchless banking innovations, namely: mobile banking, agency banking, internet banking and automated teller machines. These financial innovations represent a departure from traditional branch based banking. We conduct an empirical analysis of the four financial innovations using Koyck distributed lag models, estimated using dynamic panel estimation with System Generalized Method of Moments. We use 10-year panel data from 42 out of 43 commercial banks in Kenya covering the years 2004–2013. We provide empirical evidence that at the firm level, branchless banking is driven by firm size, transaction cost, agency costs, technological developments at the firm level and firm constraints. In addition, at the macro level, regulation, technological developments at the macro level,

incompleteness in financial markets and globalization are important drivers of branchless banking.

#### KEYWORDS:

Financial innovation   financial innovation drivers   branchless banking models   network externalities

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## Disclosure statement

No potential conflict of interest was reported by the authors.

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## Notes

1. Licensed to the University of the Witwatersrand.
  2. The stock-market development index (SMINDEX) comprises a number of listed companies, market capitalization, value of shares traded and turnover ratio. For details on the construction of this indicator, see Mahonye ([2014](#), pp. 100–102).
  3. Internet banking data (deposit accounts) was not available for 2004–2008.
  4. Kenswitch is a shared financial switch comprising a consortium of over 20 Kenyan commercial banks that enable the round-the-clock delivery of electronic banking services through the use of a range of delivery channels. It was established with the key objective of “creating a common switch and ATM network between various small and medium sized banks in Kenya” (LTS, [2015](#)).
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## Additional information

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