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Anti-Money Laundering Training and Profitability of Commercial Banks in Kenya

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Abstract

The commercial banks' profitability has experienced fluctuations over the past decade. The study sought to determine the effect of anti-money laundering training on the profitability of commercial banks in Kenya. The research employed an explanatory research design. The targeted population comprised 35 regulated commercial banks as at December 31, 2021. The study period was eight (8) years (2014 to 2021). Respondents were chosen through purposive sampling. Primary data was gathered using structured questionnaires, while secondary data was derived from the annual banking supervision report from the Central Bank of Kenya. Data was analyzed using descriptive statistics and regression analysis. The findings revealed that anti-money laundering (AML) training had a positive and significant effect on the profitability of commercial banks ($\beta = 0.222$, p-value $= 0.005 < 0.05$). The study concludes that employing and retaining employees with adequate anti-money laundering skills improves the proactiveness of banks in identifying and preventing potential money laundering activities. Commercial banks should institutionalize structured AML training programs by implementing both on-the-job and off-the-job together with assessments to validate employee understanding and competency.

Keywords: *Anti-money laundering training, Profitability, Commercial Bank*

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1. Introduction

Commercial banks play a critical role in the global economy by facilitating the efficient allocation of financial resources and acting as intermediaries channeling funds from surplus sectors to sectors with funding deficits (Ongore & Kusa, 2013). According to Saona (2011), a stable and effective financial system enhances bank profitability through increased availability of investment funds. This promotes economic growth by directing savings toward productive sectors (Alkhazaleh & Almsafir, 2014). However, inadequate risk management practices can significantly undermine the profitability of commercial banks, particularly those with limited resources (Makokha *et al.,* 2016). Maintaining profitability is essential for commercial banks to fulfill their intermediary role and ensure long-term sustainability (Odhiambo, 2019). As Levine (1997) asserts, the stability of commercial banks depends on their ability to effectively perform core economic functions, such as deposit mobilization, savings allocation, trade facilitation, risk management, and credit provision.

Tariq *et al.* (2014) emphasize that profitability is vital for banks to remain competitive and operational in today's dynamic financial landscape. In Kenya, the banking sector has undergone significant transformations over the past two decades, with commercial banks striving to enhance their financial performance amid changing economic conditions (Omondi, 2019). However, performance has remained inconsistent, as illustrated by fluctuating returns on equity: from 24.3% in 2015 to 20.7% in 2017, a slight recovery to 22.5% in 2018, and a notable drop to 13.9% in 2020. These trends raise concerns, especially considering the various reforms implemented to bolster performance. Al-Qudah and Jaradat (2013) observe that the operating environment for commercial banks is continuously evolving, and profitability remains a crucial indicator of financial health.

The International Monetary Fund (2021) underlines the importance of well-regulated and well-supervised financial systems in supporting domestic and international financial stability. Effective AML frameworks enable commercial banks to mitigate reputational, operational, and legal risks that can erode financial performance (Arnone & Padoan, 2008). Banks with strong compliance programs are less likely to incur regulatory fines, suffer reputational damage, or lose customer confidence, all of which contribute to stable earnings and long-term viability (Wehinger, 2011). FATF (2020) upholds that AML compliance enhances institutional integrity by fostering transparency and accountability accordingly boosting investor and customer trust. Therefore, robust AML practices protect banks from systemic shocks, facilitate cross-border operations, and preserve access to international financial markets factors that are essential for sustaining profitability in a competitive global landscape (World Bank, 2017).

According to Gatete (2015), profitability is the bank's ability to generate income in excess of all its expenses. Velnampy and Niresh (2012) indicate that commercial banks' primary objective is to make a profit, this designates management's capacity to utilize the firm resources to generate profits (Muya & Gathogo, 2016). Ayanda *et al*. (2013) point out that a successful business should be able to steadily sustain its profits. However, Horton (2018) contends that a profitable business may not necessarily be a sound and profitable one in reality. Therefore, the profitability of a commercial bank is its effectiveness in generating earnings (Podder, 2012). Nevertheless, simply having large overall capital, investments, receivables, or assets does not necessarily translate to profitability in commercial banks (Tarawneh, 2006). The standard of a bank's earnings and profitability profile determines whether it can support its current and future activities (Shar *et al*., 2011).

According to Leong (2007), educating bank officials is crucial to guarantee that the staff understands the entire anti-money laundering realm and empowers them to identify, measure, monitor, and control threats related to money laundering practices. Rothwell and Kazanaz (1994) highlight that employee training can take place either at work or away from it. At-the-work training enhances employee's skills while they work, whereas off-the-work training takes place outside of the employee's regular work environment (Malone, 1984). Training enhances the bank's proactiveness in detecting and preventing probable money laundering activities. Nunes *et al*. (2014) suggest that increased awareness of money laundering can reduce the likelihood of individuals becoming conduits for such illegal activities. Similarly, Kathuli (2018) underscores that a significant barrier to effectively combatting money laundering is inadequate training and deficient technical skills. POCAMLA (2009) mandates that commercial bank executives and employees must undergo training on anti-money laundering practices.

1.1 Problem Statement

Njung'e (2019) maintains that commercial banks are institutions established on profit-making strategy to enhance shareholder value while contributing to economic growth. The Kenyan economy is heavily reliant on the banking sector, and its failure negatively affects the entire economy (Kamau, 2009). Profitability remains a fundamental objective for commercial banks, with all strategic and operational decisions geared toward maximizing financial returns (Ongore & Kusa, 2013). According to Brigham and Houston (2012), enhancing shareholder value is the primary goal of any firm, reinforcing the importance of sustained profitability as a measure of success.

However, in Kenya, commercial banks' profitability has experienced fluctuations over the past decade, as evidenced by a decline in profit before tax from Kshs. 147.4 billion in 2016 to Kshs. 133.2 billion in 2017 (Central Bank of Kenya, 2017). This downward trend has occurred in parallel with increasingly stringent regulatory requirements, particularly in the implementation of Anti-Money Laundering (AML) practices. This practice imposes significant operational and financial burdens on banks including the cost of compliance programs, staff training, transaction monitoring, and regulatory reporting. This process can be costly and resource-intensive, and it may not always directly align with the actual risk of money laundering (KPMG, 2014; Geiger & Wuensch, 2007). As a result, there is growing concern about whether the implementation of AML practices negatively impacts bank profitability or on the contrary, if it augments long-term performance by mitigating AML risk, improving customer and shareholder trust, and ultimately enhancing profitability.

Numerous studies have investigated the link between anti-money laundering practices and the profitability of commercial banks, both locally and globally. For instance, Idowu and Obasan (2012) analyzed the impact of anti-money laundering policy on the financial performance of institutions in Nigeria. Khrawish (2014) examined the influence of AML on funding investments in Jordanian financial institutions. Wario (2013) conducted an assessment of the efficacy of AML regulations. The research concentrated on two Tanzanian banks, namely the Cooperative Rural Development Bank (CRDB) and the National Bank of Commerce (NBC). Similarly, Commey (2019) explored the connection between Ghanaian commercial banks' performance and anti-money laundering laws. However, these studies were conducted in different places outside of Kenya. Therefore, the results may not apply to the local economic environment since the social, economic, and legal environment of global studies differs from that of Kenya.

Locally, several studies were conducted in Kenya by Murithi (2013), Michugu (2014), Sainah (2015), and Mohamud (2017), focusing on the relationship between anti-money laundering (AML) regulations and financial performance. Murithi (2013) examined the impact of implementing AML regulations but limited the analysis to regulatory enforcement, without addressing the broader implications of AML practices. Michugu (2014) assessed the effect of AML regulations on the financial performance of Chase Bank. However, the study focused on a single institution. Sainah (2015) explored the impact of anti-money laundering risk assessments on the performance of commercial banks in Kenya however, the study did not reveal a direct impact on profitability measured by return on equity. Mohamud (2017) analyzed the effect of AML risk management on the financial performance of commercial banks in Kenya but did not consider the effect of corporate governance as a moderating factor.

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Additionally, there was a lack of sufficient empirical data to assess how AML practices influenced the profitability of commercial banks in Kenya, particularly the changes observed over the period from 2014 to 2021. This study specifically sought to determine the effect of anti-money laundering training on the profitability of commercial banks in Kenya.

1.2 Research Hypothesis

H_{01}: Anti-money laundering training has no significant effect on the profitability of commercial banks in Kenya.

2. Literature Review

2.1 Theoretical Review

Kane first introduced the Regulatory Dialectic Theory (RDT) in 1977. The theory advances a recursive relationship between financial institutions and government regulatory agencies (Kane, 1977). According to Levi-Faur (2011), regulatory dialectic theory is a framework that explains the complex interactions between regulators and the institutions they govern. Hood (2006) suggests that regulatory dialectic theory is particularly useful for understanding how regulation evolves in dynamic and rapidly changing fields like technology and finance. Awrey (2012) notes that the theory takes into account how financial institutions respond to various factors such as changes in technology, political forces, market dynamics, laws, and regulations. Sinkey later expanded on the theory in 1992 by connecting it to exclusionary rules, specifically regulations that lead to the creation of financial institution markets that are non-competitive (Currie, 2002). As a result, ongoing negotiation and compromise shape the regulation over time (Kane, 1977).

Moore (1995) suggests that regulation is not a fixed outcome, but instead a continuously developing process shaped by various actors and institutions. This process involves ongoing negotiation and compromise between the regulatory body and commercial banks, resulting in changes in regulation over time. Acharya *et al*. (2010) assert that the regulatory process is epitomized through the adoption of new markets, products, and/or services. This phenomenon was exemplified by the expansion of shadow banking before the 2007 Financial Crisis, driven by banks' efforts to avoid close regulatory oversight (Thiemann, 2014). Equally, Mayes and Wood (2007) observed this trend in their research on offshore financial centers. They argue that despite the regulations, some institutions have been able to circumvent the rules. Kane (1988) contends that organizational learning and market-driven incentives for bank management cause the cycle of dodging and re-regulation, which results in less effective anti-money laundering directives.

Pol (2009) posits that the Regulatory Dialectic Theory implies that commercial banks are likely to participate in money laundering operations, even when they are subject to regulations. This theory submits that the prevention of money laundering within the financial system may be impeded by rogue commercial banks motivated to evade regulations to maximize their profits. Consequently, the implementation of new regulations may trigger the development of innovative methods for evading business constrictions, including anti-money laundering laws. As a result, regulators face a constant challenge, as they must keep up with the ever-changing tactics used by criminals and rogue actors within the commercial banking sector. Consequently, regulatory dialectic theory provides a link between AML training and profitability where bank internal governance mechanisms shape the effectiveness of externally imposed AML regulations.

2.2 Empirical Review

Nafula (2019) conducted a research investigation focusing on the challenges encountered when trying to put in place efficient anti-money laundering strategies. Conclusions observed that training both new and current employees to identify suspicious activities in a banking environment requires time and resources. The study specifically examined the obstacles encountered in implementing successful anti-money laundering strategies in commercial banks but did not factor in the ROE profitability metric ratio. However, this research sought to determine how AML practices affect profitability, evaluated using the ROE metric.

Kemal (2014) analysed the role of employee training in strengthening the financial system's ability to detect and combat money laundering. Exploratory research study was utilized to investigate and analyse key variables. A sample of 100 responses was gathered from Pakistani bank employees working in various institutions. The analysis found a statistically significant positive relationship between staff training and the ability of financial institutions to recognize and report suspicious financial transactions. The study was conducted for a financial institution based in Pakistan. However, in this study commercial banks in Kenya are the main unit of analysis.

Murithi (2013) examined the impact of implementing anti-money laundering (AML) regulations on the financial performance of commercial banks in Kenya. The study focused on 31 commercial banks and utilized both primary and secondary data collected through questionnaires and financial reports. The findings revealed that while compliance with AML regulations led to increased operational costs, such as training and enhanced reporting obligations, it had a positive influence on the bank's financial performance. This study focused on the financial performance measured by return on assets. The current study focuses on the profitability measured by return on equity to assess bank's ability to generate profits from shareholders' equity.

Commey (2019) assessed how compliance with anti-money laundering regulations influences the operational outcomes of commercial banks in Ghana. The research findings indicated a positive influence of anti-money laundering compliance on the profitability of these banks. Additionally, it was noted that a deficiency in trained and skilled personnel hindered the effective implementation of anti-money laundering programs in Ghanaian commercial banks. The primary focus of the study was on understanding how adherence to AML regulations affected the commercial banks' performance in Ghana, however, the proposed study is centered on a Kenyan setup.

3. Methodology

The study employed an explanatory research design. The target population consisted of thirty-five (35) commercial banks as at December 31, 2021. The study period was eight (8) years (2014 to 2021). Respondents were chosen through purposive sampling. Primary data was gathered using structured questionnaires, while secondary data was derived from the annual banking supervision report from the Central Bank of Kenya. The data was analyzed using descriptive statistics and regression analysis.

4. Results and Discussion

4.1 Descriptive Analysis for Anti-money Laundering Training

Table 1 presents the results of the AML training descriptive analysis.

Table 1: Anti-money laundering training

Statement N=77	SD	D	N	A	SA	M	Std dev
The bank employs and retains employees with adequate anti-money laundering skills.	11.7%	13.0%	1.3%	26.0%	48.1%	3.9	1.4
Professionally trained and motivated employees can implement anti-money laundering practices.	1.3%	9.1%	7.8%	55.8%	26.0%	4.0	0.9
All bank staff are trained and assessed to confirm understanding.	3.9%	14.3%	5.2%	28.6%	48.1%	4.0	1.2
Enhanced staff training improves the proactiveness of banks in identifying and preventing potential money laundering activities.	3.9%	2.6%	2.6%	54.5%	36.4%	4.2	0.9
Anti-money laundering training fosters the necessary skills required to manage the risks related to occurrences of money laundering.	2.6%	19.5%	18.2%	24.7%	35.1%	3.7	1.2
Overall mean						**3.9**	**1.1**

Based on the findings presented in Table 1, the majority of respondents agreed with several key statements regarding anti-money laundering (AML) training in Commercial banks in Kenya. They agreed that the bank employs and retains employees with adequate anti-money laundering skills (M = 3.9), that professionally trained and motivated employees can implement anti-money laundering practices (M = 4.0), and that all bank staff is trained and assessed to confirm understanding (M = 4.0). Furthermore, the respondents concurred that enhanced staff training improves the proactiveness of banks in identifying and preventing potential money laundering activities (M = 4.2). They also agreed that anti-money laundering training fosters the necessary skills required to manage the risks related to occurrences of money laundering (M = 3.7). Nafula (2019) emphasized that equipping both new and existing employees with the ability to identify suspicious activities within the banking environment requires substantial time and resources. Similarly, Wright, Kroll, and Tokle (2001) argued that AML training enhances employees' capabilities to proactively detect and prevent illicit financial activities, reinforcing the role of human capital as a critical strategic asset in combating financial crime. The overall average mean score of 3.9 indicates that most participants agreed on the significance of AML training as a critical practice that can enhance profitability. Additionally, the low standard deviation of 1.1 suggests relatively minor variability in responses.

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4.2 Descriptive Analysis for Profitability of commercial banks in Kenya

Table 2 shows profitability trends among commercial banks operating in Kenya between 2014 and 2021.

Table 2: Profitability of commercial banks in Kenya

	N	Mean	Std. Deviation	Minimum	Maximum
ROE	280	7.41	36.42	-376	82.1

Table 2 presents the profitability trends of commercial banks, evaluated through return on equity (ROE), revealing an average annual ROE of 7.41% over the 2014–2021 period.

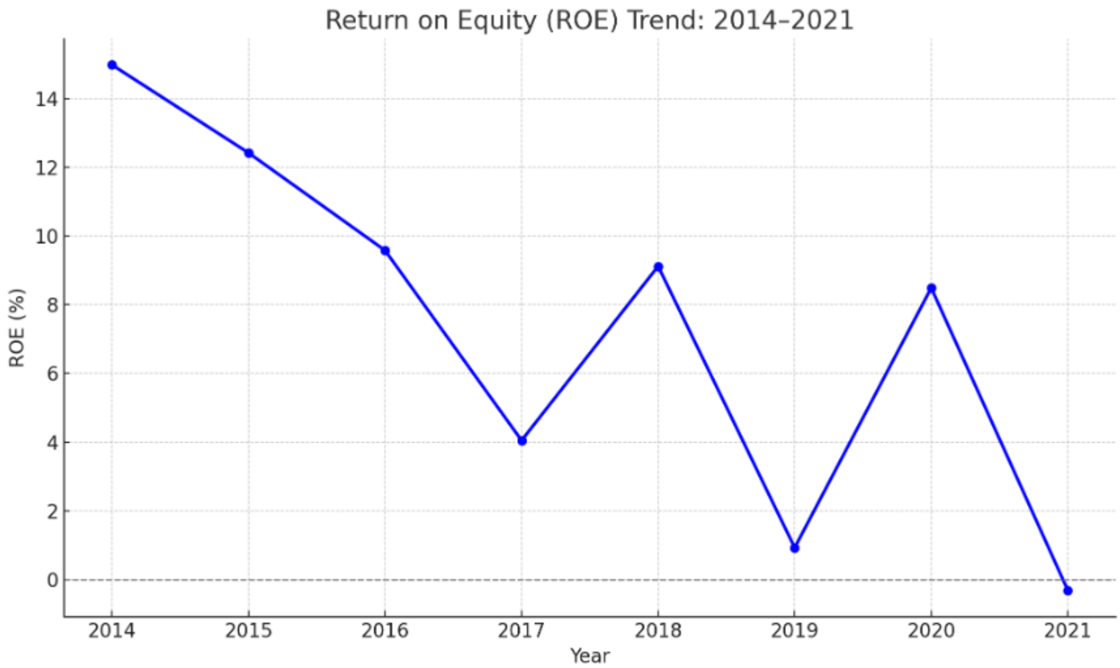

Figure 1: Return on Equity Trend

Figure 1 presents the Return on Equity (ROE) trend from 2014 to 2021, highlighting a sustained decline between 2014 and 2017, intermittent recoveries in 2018 and 2020, and a sharp downturn resulting in negative ROE in 2021. This pattern indicates that banks struggled to generate adequate returns, potentially due to reduced profitability and increased compliance costs related to anti-money laundering measures, which may have impeded efficient resource utilization.

4.3 Regression Analysis

A regression analysis was conducted to investigate the effect of anti-money laundering training on the profitability of commercial banks in Kenya.

Table 3: Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-0.241	0.304		-0.792	0.431
	Anti-money laundering training	0.222	0.077	0.233	2.887	0.005

a Dependent Variable: Profitability

According to Table 3, the statistical analysis revealed that anti-money laundering (AML) training had a positive and significant effect on the profitability of commercial banks ($\beta = 0.222$, p-value $= 0.005 < 0.05$). This indicates that a one-unit increase in AML training corresponds to a 0.222 unit increase in profitability. Consequently, the null hypothesis (H03), which posits that AML training has no statistically significant effect on the profitability of commercial banks in Kenya, is rejected. These findings align with those of Kemal (2014), who underscored the critical role of employee training in enhancing the effectiveness of AML measures, emphasizing that well-trained staff are more proficient in identifying and addressing money laundering risks. In contrast, Murithi (2013) found that AML compliance particularly the costs associated with staff training had a negative impact on bank performance, largely due to the financial strain such compliance places on institutions.

5. Conclusion

The findings established that anti-money laundering (AML) training had a significant and positive effect on the enhancement of the bank's profitability. Therefore, employing and retaining employees with adequate anti-money laundering skills improves the proactiveness of banks in identifying and preventing potential money laundering activities. This submits that anti-money laundering (AML) training is a crucial element of anti-money laundering practices and significantly contributes to profitability of commercial banks, particularly focusing on anti-money laundering (AML) training programs that is on-job and off-the-job training.

6. Recommendations

The study revealed that anti-money laundering (AML) training significantly and positively affects profitability. Therefore, Commercial banks should institutionalize structured AML training programs by implementing both on-the-job and off-the-job together with assessments to validate employee understanding and competency. These training initiatives should aim to equip staff with up-to-date knowledge and practical skills to effectively fulfill their AML responsibilities, ensuring consistent compliance and operational effectiveness.

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