COMPETITIVE STRATEGIES AND PERFORMANCE OF COMMERCIAL BANKS IN KENYA

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DECLARATION

I, the undersigned declare that this is my original work and has not been presented for a degree in any other college, institution or university.

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This research project has been submitted for examination with my approval as the university supervisor

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May God bless you all abundantly.

DEDICATION

To dad & mum, my loving husband Jimmy and our children Eric and Wanja for their love and cheerful support.

ABSTRACT

The primary objective of profit-making organizations is to maximize the performance of the organization overtime. Superior performance can be achieved in a competitive industry through the pursuit of a generic strategy, i.e. the developments of an overall cost leadership, differentiation or focus approach to industry competition. Also, following the recent global credit crunch, profitability of commercial banks is considered very crucial, thus the present study's objective is to examine the relationship between competitive strategies and profitability of commercial banks in Kenya.

The study used the survey method to assist in achieving the objective of the study. The population of the study consisted of all the 44 commercial banks operating in Kenya as at 31st December 2009. Primary data was gathered using questionnaires administered to corporate strategy managers and operations managers of the various banks. Out of the 44 banks targeted, 38 responded by returning filled questionnaires. This formed an 86% response rate thus considered suitable for analysis. To achieve the study objective, respondents were issued with a number of competitive strategies and were required to score on a 5-point likert scale the extent to which the strategies were adopted by their respective banks. The study scope allowed for only three strategies that formed the conceptual framework of the study and the data to be tested. Secondary data, in the form of the various performance measures (i.e. Profitability ratios, capital and risk weighted assets ratios and market share ratios) for the period 2005 to 2009 was collected from the financial statements of banking institutions operating in Kenya as well as from the Central Bank of Kenya's website. The study used descriptive and inferential statistics to

arrive at a more in-depth profile in establishing the link between competitive strategies adopted and firm performance indicators.

The study was able to establish that despite the challenges in implementation, competitive strategies are very important for banks to remain competitive in the market. In the banking industry, understanding the market structure is a key determinant for the successful implementation of the competitive strategies. Banks following a cost leadership strategy realize statistically significant superior performance compared to those that pursue broad differentiation and focus strategy which report above average returns. The differentiation strategy may be difficult to implant in a service industry since services are easily copied and fruitful options may be limited due to the simplicity and imitability of financial services, unless the target market is highly sophisticated and knowledgeable. The researcher highly recommends that commercial banks consider shifting more of their focus to the cost leadership strategy in order to realize superior performance.

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CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Organizations exist as open systems hence they are in continuous interaction within the environment in which they operate. The environment is highly dynamic, chaotic & turbulent such that it is not possible to predict what will happen and/or when it will happen. Consequently, the ever-changing environment continually presents opportunities & challenges. Thus to ensure survival and success, organizations need to develop capability and capacity to manage threats and exploit the emerging opportunities promptly. This requires formulation of strategies that constantly match capabilities to the environment's requirements. Success therefore calls for a proactive approach to business (Pearce & Robinson, 2003). These strategies are referred to as competitive strategies.

A competitive strategy refers to choices as to how an organization positions itself in relation to competitors. It is not possible to reduce uncertainty sufficiently to arrive at a clear strategic position upon which strategies can be rationally evaluated. However, the ambiguity and uncertainty of the future may be beneficial in that it can give rise to a variety of different perspectives that can stimulate new ideas from within and around the organization. Organizations are, therefore, undertaking strategic changes in order to align their business strategies to the environment thereby matching resources and activities of an organization to that environment (Johnson and Scholes, 2002).

The banking sector registered good performance in 2009 notwithstanding local and global turbulence. Going forward, the sector's growth trajectory is expected to increase in the backdrop of new opportunities in the domestic and regional markets. On the domestic arena, new opportunities are expected to be created by the adoption of agent banking, credit information sharing and mobile phone technology innovations. Institutions are also expected to explore and venture into regional markets as regional integration initiatives intensify (CBK, Bank Supervision Annual Report 2009).

In order to be successful, organizations must be strategically aware. They must understand how changes in their environment are unfolding. They should actively look for opportunities to exploit their strategic abilities, adapt and seek improvements in every area of business, building on awareness and understanding of current strategies and successes. To succeed in the long-term, organizations must compete effectively and outperform their rivals in a dynamic environment.

1.1.1 Competitive Strategies

Competitive strategy is the search for a favourable competitive positioning in an industry, the fundamental arena in which competition occurs. Competitive strategy is concerned with how a company can gain a competitive advantage through a distinctive way of competing. It aims to establish a profitable and sustainable position against the forces that determine industry competition. According to (Porter, 1980), developing a competitive strategy is developing a broad formula on how a business is going to compete, what its goals should be and what policies would be needed to carry out these goals. He looked at competitive strategy as a combination of the ends (goals) for which the firm is striving & the means (policies) by which it is seeking to get there.

Every organization should have a competitive strategy. However, many organization's strategies are implicit, having evolved overtime, rather than explicitly formulated from thinking and planning process. Implicit strategies lack focus, produce inconsistent decisions and unknowingly become obsolete. Without a well defined strategy, organizations will be driven by current operational issues rather than by a planned future vision. Excellent competitive strategies should be business oriented and able to address the core business of the organization. The intensity of competition in an industry in an industry determines its profit potential and competitive attractiveness and therefore the strategy should be able to spell out how the organization responds to the competitive forces in these industries or markets (Dierickx, 1989).

The purpose of competitive strategy is to achieve a sustainable competitive advantage and thereby enhance a business performance (Bharadwaj, 2003). As such organizational competitive strategies serve to improve organizational performance of the firm through the route of sustainable competitive advantages. Studies in the field of strategic management have shown that in most industries, some firms are more profitable than others regardless of whether the average profitability of the industry is high or low. The superior performers conceivably possess something special and hard to imitate that it allows them to outperform their rivals. These unique skills and assets (resources) are referred to as a source of competitive advantage which can result from implementing a value creating strategy not simultaneously being implemented by any current or potential competitors; or through superior execution of the same strategy as competitors. Sustainability is achieved when the advantage resists erosion by competitors' behavior. In other words, the skills and resources underlying a business' competitive advantage must resist duplication by other firms.

1.1.2 Firm Performance

Performance has improved tremendously as banks continue to report very good returns in their annual financial statements. This is as a result of the fact that in the recent past, the economy has enjoyed a favourable macroeconomic environment consistent with low and stable interest rates, strengthening shilling exchange rate and falling inflation. The stability of the sector is attributed to the stable macro- economic environment and improved supervisory oversight. The general outlook of the sector is positive in view of the adequate capitalization, sound risk management systems, strong asset quality and profitability, (CBK, Bank Supervision Annual Report 2009).

During the period ended 31st December 2009, the Kenyan Banking Sector registered a significant growth in asset base largely supported by growth in deposits, injection of capital and retention of profits. The sector registered high capital adequacy and liquidity ratios and a decline in the level of non-performing loans compared to 2008. The overall performance of the banking sector was rated strong in December 2009; a similar rating was attained in December 2008. The Total net assets grew by 14.3%, customer deposits increased by 16.4% and profit before tax rose by 12.9% compared to performance in 2008. Institutions maintained capital adequacy ratios above the minimum requirements of 12.0%. However, return on equity dropped to 24.9% from 26.1% registered in December 2008 occasioned by an increase in equity at a higher rate than increase in income. The overall performance of the banking sector rated strong in December 2009, a similar rating attained in December 2008, (CBK, Bank Supervision Annual Report 2009).

The Central Bank of Kenya (as the regulatory authority), applies the CAMEL rating system to assess the soundness of financial institutions which is an acronym for Capital

Adequacy, Asset Quality, Management Quality, Earnings and Liquidity. In its market share analysis, institutions were classified into the following three peer groups based on asset size: Large with assets above Kshs. 15 billion, medium with assets valued at between Kshs. 5 billion and Kshs. 15 billion and Small with assets valued at less than Kshs. 5 billion. Nineteen (19) financial institutions were classified as large, fourteen (14) institutions were medium and twelve (12) institutions were small. Going forward, the sector's growth trajectory is expected to increase on the backdrop of new opportunities in the domestic and regional markets. On the domestic arena, new opportunities are expected to be created by the adoption of agent banking, credit information sharing and mobile phone technology innovations. Institutions are also expected to explore and venture into regional markets as regional integration initiatives intensify, (CBK, Bank Supervision Annual Report 2009).

The Central Bank of Kenya has made it mandatory for Commercial banks to publish their quarterly financial statements in a newspaper of nationwide circulation. It stipulates a format to be adopted by all the players in the industry. Under the disclosure section of the financial statements, one is able to derive the non-performing loans & advances, insider loans & advances, off-balance sheet items, capital strength as well as the liquidity levels as presented using ratios. The interested parties may also derive from the main accounts the performance levels by checking the levels of growth in assets, deposits and profitability. Noting that eight of the major banks in Kenya have been listed in the Nairobi Stock Exchange (NSE), its shareholders may want to measure their return through use of ratios. A high Price Earnings ratio (P/E) ratio for instance would be an indication of strong investor confidence in a firm's outlook and earnings growth. The dividend yield on the other hand measures the return that shareholders receive from dividends.

1.1.3 Banking Industry in Kenya

The banking industry comprised the Central Bank of Kenya, Commercial Banks, Non-Banking Financial Institutions, Forex Bureaus and Deposit- taking Microfinance Institutions as the regulated entities. As at 31st December 2009, the banking sector was composed of 46 institutions, 44 of which were commercial banks and 2 mortgage finance companies. In addition, there was 1 licensed deposit-taking microfinance institution and 130 foreign exchange bureaus. Out of the 46 institutions, 33 were locally owned and 13 were foreign owned. The locally owned financial institutions comprised 3 banks with public shareholding, 28 privately owned commercial banks and 2 mortgage finance companies. The foreign owned financial institutions comprised 9 locally incorporated foreign banks and 4 branches of foreign incorporated banks (CBK Report on Bank Performance, 2009). Established in 1966 through an Act of Parliament, the CBK, acting as the overseer of the other financial institutions has the objective of formulating and implementing the monetary policies directed to achieving & maintaining stability in the general level of prices; fostering liquidity, solvency and proper functioning of a stable market-based financial system; and licensing and supervising authorized dealers in the money market.

There have been a lot of changes in the banking industry since the 1980s. Financial modernization, de-regularization, industry consolidation, the rise of new institutions, shifting trends in borrowing and lending, globalization and emerging technology have influenced and affected how commercial banks operate. The evolution of the banking industry has presented both challenges and opportunities for commercial banking institutions and as such, only those with the best mix of products and services do survive.

Commercial banks have embarked on various changes aimed at repositioning themselves as modern. This has involved rebranding e.g. changing of the corporate colours and logo as done by NIC bank and Barclays Bank of Kenya among others. Commercial banks are also rapidly expanding their branch networks (The Standard, December 18, 2007). The NIC Bank, through its 'MOVE' slogan repositioned itself as a retail bank away from its earlier position as a corporate bank. Many banks have also made their operations more flexible by extending their official working hours as well as creating lounges for their corporate clients.

Commercial banks have also sort to massively increase their range of services. For instance, most major banks have begun providing mortgage services and investment banking services. In the recently held Safaricom initial public offering (IPO), most banks were involved and were especially keen to offer loans to the investors. Leading the pack was the Equity bank who mobilized applications worth Kshs 37 Billion representing 45% of those allowable for local investors. This led to opening of a lot of new accounts to the benefit of the bank.

Through product-service innovation, banks are attempting to achieve a finer degree of control over financial risks and thus minimizing any impending losses. Most major banks have introduced 'check off' unsecured personal loans, which lend directly to employees of large institutions with loan deductions coming directly from the employer. Some have even introduced a cheaper deposit account with a single tariff.

In order to effectively compete, a number of mergers and acquisitions have taken place especially among the smaller industry players, the most recent acquisition being that of Southern Credit Banking Corporation by Equatorial Commercial Bank towards the end of June 2010. Most of these were occasioned by the need to meet the increasing minimum core capital requirements and to enhance the institutions’ market share in the local banking environment.

The market share of large banks has been growing and is expected to increase. However, there is an indication that our economy is maintaining a strong and active sector of the smaller community banks meeting the needs of households and small businesses. Possible curtailment of credit to small businesses as the banking industry becomes more concentrated is of concern but studies indicate that small banks often fill the voids left by their larger counterparts.

The commercial banks and some non-banking commercial institutions have come together under the Kenya Bankers’ Association (KBA) which serves as a lobby for the banks’ interests and also addresses issues affecting its members. The key issues affecting the industry are: changes in the regulatory framework where liberalization exists but the market still continues to be restrictive; declining interest margins due to customer pressure; increased demand for non-traditional players who now offer financial services products.

1.2 Statement of the Research Problem

Competitive performance is the main motivation to establish any business and banks are not an exception. By knowing the variables that affect a bank’s profit, the bank’s management can concentrate their efforts to optimize these variables and take them into consideration during decision making.

In a modern market economy, the banking industry is one of the crucial elements in the financial market and is reputed as the engine of growth in any country's economy. It is therefore vital for banks to operate in an efficient manner in order to create a more financially sound market environment. Arguably, this will attract a greater amount of intermediate funds to the banks as more customers go to the banks and hence increase profitability for better financial products and services. The banking industry has been facing a myriad of challenges in the recent past ranging from loss of cash in transit to money laundering, hyper competition, unstable interest rates and loan defaulting among others. The banking industry has encountered numerous opportunities as well. Over the last several years, financial modernization, de-regularization, industry consolidation, the rise of new institutions, shifting trends in borrowing and lending, globalization and emerging technologies have influenced how commercial banks operate.

Competitive advantage is realized based on three factors (Berger, 2005): The firm's formulated strategies; Implementation of these strategies; and the industry context (Porter's model). An important component of a firm's strategy is the relationship with the overall performance of that organization. Competitive strategies in the banking industry are essential especially in the developing countries since they serve as the nerve for overall financial development in terms of economic growth at the macro level (Andersen and Trap, 2003). However, there are no clear measurements and determinants of competitive strategies in the banking industry towards sustainable growth due to intense competition and copying strategies among competitors.

Locally, various studies have been conducted on strategies adopted by various companies. Mungai (2008), studied choice of strategy in a competitive environment – case of Equity bank; Muhindi (2007), studied response strategies to increased competition by insurance companies; Shikanga (2006), studied marketing strategies in the Kenyan motor vehicle industry and yet another study by Njuguna (2005) focused on environmental changes and their influence on small and medium enterprises. Various literature related to commercial banks also exist locally (Mbayah, 2008; Ngare, 2008; Muturi, 2005; Gachiri, 2008). None of these studies assessed the relationship between competitive strategies adopted and the performance of commercial banks in Kenya. This research was therefore aimed at establishing the relationship between competitive strategies and the performance of commercial banks in Kenya.

1.3 Research Objective

The objective of this study was to establish the relationship between competitive strategies and the performance of commercial banks in Kenya.

1.4 Significance of the Study

The area relating to banks' competitive strategies especially in Kenya is still suffering from a deficiency of information since there are few studies that have adequately discussed this issue. This study is expected to contribute to the literature in existence and will go a long way to facilitate further understanding into the area. This will particularly be helpful to the scholars in the area and the banking industry stakeholders.

The government and other institutions (like the Central Bank of Kenya) involved in policy formulation will find the findings of this research useful since it will contribute towards the formulation of positive fiscal policies that are relevant to the forces influencing the banking industry's performance in Kenya.

Finally, other researchers & banking institutions willing to highlight competitive strategies in the banking industry while describing its relevance in the developing countries will also find this study resourceful.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

In this chapter, previous studies related to the topic are reviewed. The chapter begins with literature on competitive strategies, firm performance and also discusses performance measurement.

2.2 Competitive Strategies

Competitive strategy refers to how a firm competes in a particular industry. Competitive strategy is concerned with how a company can gain a competitive advantage through a distinctive way of competing. For a firm to have a competitive advantage, it has to have a business strategy that improves the competitive position of its products and services. A business strategy can be too competitive if it involves battling out with other competitors or cooperative, working with one or more competitors to gain advantage against other competitors or both, (Johnson & Scholes, 2003).

To sustain a competitive advantage, a firm must keep learning how to do things better and keep spreading that knowledge throughout its organization. Firms must leverage the power of knowledge. (Day and Wensley, 1988) argue that all knowledge is not the same and that there is explicit knowledge that can be written down. Such knowledge as patents, procedures, formulations or engineering designs are referred to as explicit. Tacit/implicit knowledge is far less tangible and is deeply embedded into an organization's operating practices. This may be referred to as the organizational culture. Compared to explicit knowledge, implicit knowledge can be a sustainable source of competitive advantage that is quite difficult for competition to emulate.

(Ansoff , 2006) observed that for a firm to optimize its competitiveness and profitability and indeed long-term sustainability, it has to match its strategy and supporting capability with the environment. According to him, strategy formulation and strategies are context sensitive which might explain that fact that there are many competing models in strategic development and strategic planning.

Competitive strategy is the approach the company uses to present itself to the marketplace, the rules it uses to win in the market place, and the actions it takes to protect itself from competitors. Competitive strategy is a narrower scope than business strategy and focuses on management's plan of competing successfully. It consists of moves to: Attract customers; Withstand competitive pressure; and Strength firm's market position. Competitive strategy hinges on a company's capabilities, strengths, and weaknesses in relation to market characteristics and the corresponding capabilities, strengths, and weaknesses of its competitors. Competitive strategy is concerned with competitors and the basis of competition.

Competitive Strategy is the basis for much of modern business strategy. Any long term strategy must be based upon a core idea about how the firm can best compete in the market place. The popular term for this core idea is generic strategy. Many planners believe that any long-term strategy should derive from a firm's attempt to seek a competitive advantage based on one of three generic strategies: Striving for overall low-cost leadership in the industry; Striving to create and market unique products for varied customer groups through differentiation; and Striving to have special appeal to one or more groups of customer or individual buyers, focusing on their cost or differentiation concerns. Advocates of generic strategies believe that each one of these options can produce above-average returns for a firm in an industry, (Pearce and Robinson, 1997).

2.3 Generic Strategies

Competitive strategies focus on ways in which a company can achieve the most advantageous position that it possibly can in its industry. The profit of a company is essentially the difference between its revenues and costs. Therefore high profitability can be achieved through achieving the lowest costs or the highest prices vis-à-vis the competition. A firm's strengths ultimately fall into one of two headings: cost advantage and differentiation (Porter, 1980). By applying these strengths in either a broad or narrow scope, three generic strategies result: cost leadership, differentiation, and focus. These strategies are applied at the business unit level. They are called generic strategies because they are not firm or industry dependent.

While each of the generic strategies enables a firm to maximize certain competitive advantages, each one also exposes the firm to a number of competitive risks. For example, a low-cost leader fears a new low-cost technique that is being developed by a competitor; a differentiating firm fears imitators; and a focused firm fears invasion by a firm that largely targets customers. The following table illustrates Porter's generic strategies:

Table 2.1: Porter's generic strategies

Target Scope	*Advantage*	
	Low Cost	**Product Uniqueness**
Broad (Industry Wide)	**Cost Leadership Strategy**	**Differentiation Strategy**
Narrow (Market Segment)	**Focus Strategy** (low cost)	**Focus Strategy** (differentiation)

2.3.1 Cost Leadership Strategy

This generic strategy calls for being the low cost producer in an industry for a given level of quality. The firm sells its products either at average industry prices to earn a profit higher than that of rivals, or below the average industry prices to gain market share. In the event of a price war, the firm can maintain some profitability while the competition suffers losses. Even without a price war, as the industry matures and prices decline, the firms that can produce more cheaply will remain profitable for a longer period of time. The cost leadership strategy usually targets a broad market.

Low-cost leaders depend on fairly unique capabilities to achieve and sustain their low-cost position for instance, having secured suppliers of scarce raw materials and being in a dominant market share position. Low-cost producers excel at cost reductions and efficiencies. They maximize economies of scale, implement cost-cutting techniques, stress in reduction of overheads and use volume sales techniques to propel themselves up the earnings curve. A low-cost leader is able to use its cost advantage to charge lower prices or to enjoy higher profit margins.

Firms that succeed in cost leadership often have the following internal strengths: Access to the capital required to make a significant investment in production assets; Skill in designing products for efficient manufacturing (for example, having a small component count to shorten the assembly process); High level of expertise in manufacturing process engineering; and Efficient distribution channels.

2.3.2 Differentiation Strategy

A differentiation strategy calls for the development of a product or service that offers unique attributes that are valued by customers and that customers perceive to be better than or different from the products of the competition. By stressing the attribute above other product qualities, a firm attempts to build customer loyalty which often translates into a firm's ability to charge a premium price for its products. The firm usually anticipates that the higher price will more than cover the extra costs incurred in offering the unique product. Because of the product's unique attributes, if suppliers increase their prices the firm may be able to pass along the costs to its customers who cannot find substitute products easily.

The unique product attributes can also be the marketing channels through which it is delivered, its image of excellence, the features it includes and the service network that supports it. As a result of the importance of these attributes, competitors often face 'perpetual' barriers to entry when customers of a successfully differentiated firm fail to see largely identical products as being interchangeable.

Firms that succeed in a differentiation strategy often have the following internal strengths: Access to leading scientific research; Highly skilled and creative product development team; Strong sales team with the ability to successfully communicate the perceived strengths of the product; and Corporate reputation for quality and innovation.

2.3.3 Focus Strategy

The focus strategy concentrates on a narrow segment and within that segment attempts to achieve either a cost advantage or differentiation. The basis is that the needs of the group can be better serviced by focusing entirely on it. A firm using a focus strategy often enjoys a high degree of customer loyalty, and this entrenched loyalty discourages other firms from competing directly.

A focus strategy, whether anchored in a low-cost base or a differentiation base, attempts to attend to the needs of a particular market segment. Likely segments are those that are ignored by market appeals to easily accessible markets, to the ‘typical’ customer, or to customers with common applications for the product. A firm pursuing a focus strategy is willing to service isolated geographic areas; to satisfy the needs of customers with special financing, inventory or servicing problems; or to tailor the product to the somewhat unique demands of the small-to-medium-sized customer. The focusing firms profit from their willingness to serve otherwise ignored or under-appreciated customer segments.

Because of their narrow market focus, firms pursuing a focus strategy have lower volumes and therefore less bargaining power with their suppliers. However, firms pursuing a differentiation-focused strategy may be able to pass higher costs on to customers since close substitute products do not exist. Firms that succeed in a focus strategy are able to tailor a broad range of product development strengths to a relatively narrow market segment that they know very well.

Firms can make use of the focus strategy by focusing on a specific niche in the market and offering specialized products for that niche. Therefore, competitive advantage can be achieved only in the company's target segments by employing the focus strategy. The company can make use of the cost leadership or differentiation approach with regard to the focus strategy. In that, a company using the cost focus approach would aim for a cost advantage in its target segment only. If a company is using the differentiation focus approach, it would aim for differentiation in its target segment only, and not the overall market. This strategy provides the company the possibility to charge a premium price for superior quality (differentiation focus) or by offering a low price product to a small and specialized group of buyers (cost leadership focus).

2.4 Firm Performance

Performance is the accomplishment of a given task measured against preset standards of accuracy, completeness, cost and speed. Concern has been expressed, over the years; about the financial management strategies adopted by firms. Business performance measures are an important element of these financial management strategies.

This being the link between competitive strategies used to the performance achieved, it is evidenced that strategy is the game plan that creates a match between a firm’s capability and the environment. It is an action plan that a firm takes in order to achieve a set of goals. Competitive strategies guide firms to superior performance through establishing competitive advantage. In this process, companies consider alternative courses of action and choose a set of strategies for their business units. Firms employ these strategies in a dynamic environment in order to adapt to new realities such as increased competition.

Both the quantitative and qualitative criteria in the measurement of performance in firms should be taken into account when establishing a firm’s performance. When presented together, qualitative data and quantitative data can make compelling statements of program results.

Qualitative data is mainly the descriptive information from clients that is documented through open-ended questions, interviews, or structured focus groups. Details provided in these open-ended responses create a fuller picture of a program, and can add vitality to program reports. Qualitative data can add value to performance measurement by providing more in-depth information than can be obtained solely from quantitative data (numbers). Qualitative data provides more detailed descriptive information about the results being measured, as this information provides "the meaning behind the numbers”. Methods to obtain qualitative data include interviews, journals, structured focus groups and open-ended questions on surveys.

Qualitative data can be used to: Add descriptive richness to program outcomes; provide insights into why outcomes happened; Validate results measured quantitatively; Reveal unintended outcomes of your program; and provide additional information on needed improvements. Rich descriptive information provided by reporting qualitative data allows the reader to feel the impact of the program on a more personal basis, helping to contextual targets and outcomes in the program's performance measures. Some of the main qualitative measures of bank’s performance include organizational effectiveness, customer satisfaction, innovation and creativity.

Quantitative data determines the extent of an outcome in numbers. It provides an exact approach to measurement. These measures of firm performance are usually ratios fashioned from financial statements or stock market prices. Factors that have had a bearing on the resources of a firm and in turn efficient deployment are: Liquid assets; Proportion of resources deployed as investments; Proportion of resources deployed as advances; and proportion of other assets which generate relatively low yields. These have been used as the main indicators of performance in many firms. For banks, financial soundness is vital and is a situation where depositors' funds are safe in a stable banking system. The Central Bank applies CAMEL rating system to assess the soundness of financial institutions which is an acronym for Capital Adequacy, Asset Quality, Management Quality, Earnings and Liquidity.

Banks monitor adequacy of capital using ratios established by the bank for internal settlements. The banking sector capital adequacy which is measured by the ratio of Total Capital to Total Risk Weighted Assets improved in 2009. The ratio rose from 20% in December 2008 to 21% in December 2009 well above the 12% percent minimum statutory limit. The increase in capital and reserves was occasioned by fresh capital injection and retention of profits. The minimum statutory core capital requirement for banking institutions as at 31st December 2009 was Kshs 350 million and this is set to increase to Kshs 500 million by December 2010, Kshs 700 million by December 2011 and Kshs 1 billion by December 2012 (Finance Act, 2008).

The solvency of financial institutions typically is at risk when their assets become impaired therefore it is important to monitor indicators of quality of their assets in terms of exposure to specific risk trends in non-performing loans, and the health and profitability of bank borrowers. The sector registered a reduction in non-performing loans due to enhanced credit appraisal standards. However, the asset quality, which is measured by the ratio of net non-performing loans to gross loans improved marginally from 3.4% in December 2008 to 3.2% in December 2009.

Credit to Deposit Ratio and Return on Average Net Worth are some of the parameters which best reflect the quality of management based on the information available in the balance sheet. Credit to Deposit Ratio (Total advances as a proportion to total deposits) indicate management’s aggressiveness to improve income while Return on Average Net Worth (Net profit as a percentage of average net worth) is a prime indicator of management’s capability to provide adequate returns.

Continued viability of a bank depends on its ability to earn adequate return on its assets and capital. Good earnings performance enables a firm to fund its expansion and remain competitive in the market, replenish and/or increase its capital. For banks to survive, they need a higher return on assets (Earnings before interest but after tax/Average total assets) and a better return on equity (Earnings available for common stockholders/Average equity).

Liquidity which represents the ability to fund increases in assets and meet obligations as they fall due is crucial to the continued viability of any banking institution. The importance of liquidity which goes beyond the individual bank as a liquidity shortfall at an individual bank can have systemic repercussions. The liquidity ratio closed at 39.8% at the end of December 2009 in comparison with 37% reported in December 2008 and all the institutions met the minimum liquidity ratio requirement of 20%. The high liquidity ratio is as a result of the banking industry's preference to invest in the less risky government securities.

In measuring profitability of banks, bank regulators and analysts have mainly used ROA & ROE to assess industry performance and to forecast trends in market structure as inputs in statistical models to predict bank failures. Capital adequacy has also been the focus of many studies as it is considered as one of the main drivers of any financial institution's profitability. While profitability and capital adequacy measures provide significant information regarding a firm's returns, individual variables representing asset quality and earnings are informative.

2.5 Empirical studies on Competitive Strategies and Performance

Within the Kenyan context, the concept of competitive strategies has been researched on in different industry contexts: Murage, (2001) studied Competitive Strategies adopted by Members of the Kenya Independent Petroleum Dealers Association while Ndubai, (2003) studied Competitive Strategies applied by Retail Sectors of the Pharmaceutical Industry in Nairobi. Both of these studies investigated the different aspects of strategies among particular companies in Kenya.

Matengo, (2008) studied the relationship between Corporate Governance Practices and Performance: The case of Banking Industry in Kenya. The study established that not all Corporate Governance factors were important in influencing performance of commercial banks if analyzed individually.

Awiti, (2007) based her research on the Competitive Strategies used by Reproductive Health Organizations to cope with increased competition in the private sector. Her study concluded that reproductive health organizations use the following strategies to remain competitive in the market: Offering a wide range of products and services, offering free medical check-ups every once in a while, charging reasonable fees for services provided, guaranteeing security, hiring high skilled staff and establishing own hub to compete effectively.

Oyeyo, (2008) studied Sources of Competitive Advantage in the Banking Industry in Kenya. According to her research findings, a bank will achieve and sustain a competitive advantage if its personnel possess superior skills and/or capabilities; it offers high level of service quality, it has a culture that encourages continuous learning on how to do things better; it has effective leadership that is focused on continuous improvement of its value adding systems; and it is in possession of superior and/or valuable resources than the competition.

Gathai, (2009) undertook a research on the Innovation Strategies adopted by Equity Bank Ltd. She found out that in order for a firm to embrace innovation, the top management should be involved and direct resources to the team involved in the innovation process. The firm should also put in place mechanisms to compensate adequately the knowledge and also manage the same. She found out that sustainable competitive advantage should come from within the firm in form of tacit knowledge.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter contains research methodology used for the study. Research methodology gives details regarding the procedures used in conducting the study. The research design, population, data collection and analysis methods are elaborated.

3.2 Research Design

The study was carried out through a cross-sectional survey. This research design is of descriptive nature because of the nature of data collected. According to Sekaran (2003), a descriptive study is undertaken in order to ascertain and to be able to describe the characteristics of the variable of interest in a situation.

3.3 Population of Study

The population of this study consists of all commercial banks operating in Kenya. According to the Central Bank of Kenya, there were 44 commercial banks in operation as at 31st December 2009 (See Appendix II).

According to Cooper & Schindler (2003), a census survey is where data is collected from all members of the population. Census survey was appropriate for this study because the number of commercial banks is relatively small and as such, sampling was not necessary.

3.4 Data Collection

Primary data was collected by use of structured questionnaires (See Appendix I). The structured questionnaire is an efficient data collection mechanism particularly in quantitative analysis since each respondent is asked to respond to the same set of questions. The target respondents were the corporate strategy managers (or operations managers) of the banks because of their role and position which gave them the ability to effectively respond to most of the questions.

The structured questionnaire was organized into two parts where, Part A focused on the general organizational bio-data and Part B focused on establishing the extent of adoption of various selected strategies (i.e. low-cost leadership, differentiation and focus). The questionnaires were dropped and later picked from the respondents.

Secondary data was collected from the financial statements of banking institutions operating in Kenya as well as from the Central Bank of Kenya's website through the Performance Capture Forms (See Appendix III).

3.5 Data Analysis

On completion of the fieldwork, the questionnaires were adequately checked for accuracy and completeness before the analysis commenced. The data was coded, entered into a spreadsheet and version (2008) of the Statistical Package for the Social Sciences (SPSS 17.0) was used for the statistical analysis. The data was analyzed using the reliability test and frequency statistics.

Pearson Correlation Analyses was used to examine the relationship between independent variables (low-cost leadership, differentiation and focus) and the dependent variables (Firm Performance). Further, Multiple Regression dimension of independent variables and dependent variable. $Y = \alpha + \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e$; Where: X1= Low-Cost Leadership, X2 = Differentiation, X3 = Focus, β = Beta Coefficient, α = Constant and Y= Firm Performance.

CHAPTER FOUR: DATA FINDINGS AND DISCUSSION

4.1 Introduction

The data for this study was collected within two weeks using questionnaires. The questionnaires were administered to all the commercial banks all of which have their presence in Nairobi. In total, 44 questionnaires were distributed to the target population. Of these 38 questionnaires were successfully completed and collected by the researcher from the respondents at the commercial banks, giving a response rate of 86%, a percentage considered substantially sufficient for the study. Analysis of the profiles of the sample organizations was based on demographic characteristics of the respondents in terms of size of the bank, years of operation, number of employees and scope of operation.

4.2 Profile of Respective Banks

The study sought data from respondent organizations as well as from the Central Bank of Kenya on aspects that were considered to have a potential impact on the study. These aspects were in respect of the Size of the Bank (in terms of Branch Network, Number of Employees and Scope of Operation), Years of Operation, Ownership Structure and Product Range.

4.2.1 Size of the Bank

4.2.1.1 Branch Network

The study aimed at assessing the geographical branch network and the network of the 38 banks under review in this study is presented in Figure 4.1, below. Majority of these banks have 11 – 20 branches country wide indexed by 44.4%, while those with 20 and above branches indexed 40.7% and finally those with fewer branches indexed 14.8%. This clearly depicts the competition pressure within this industry.

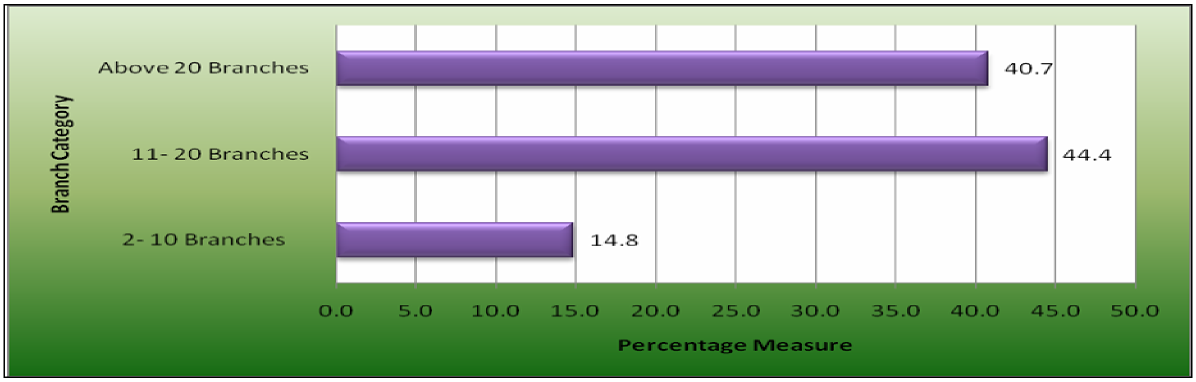

Figure 4.1: Bank Branch Size

4.2.1.2 Number of Employees

Here, the respondents even included staffs from across the Kenyan boarder. 62% of the 38 banks had a staff count of less than 1,500 employees while 24% had total employees of between 1,501 and 3,000. Finally 7% of the responses indicated that their establishment comprised of 3,001 – 6,000 employees and 7% above 6,000 employees.

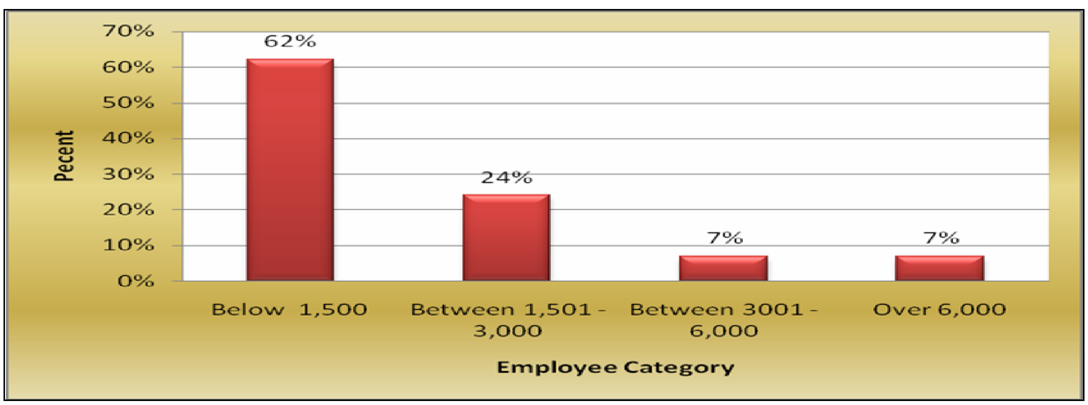

Figure 4.2: Number of Employees

4.2.1.3 Scope of Operation

Figure 4.3 illustrates the scope of operation of the commercial banks under the study. Majority of the banks have their focus on the East African region indexed by 60%. 30% of these banks have a global vision while the minority's (10%) main focus is within the domestic market.

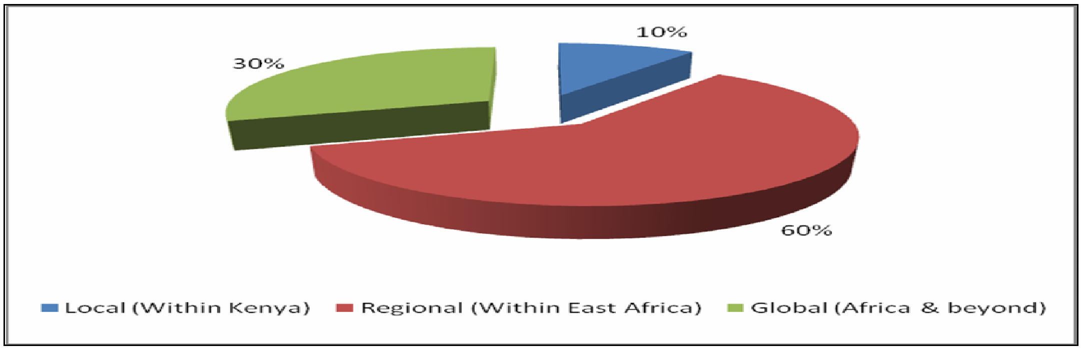

Figure 4.3: Scope of Operation

4.2.2 Years of Operation

58.0% of the 38 banks (22 banks) have been in operation for periods between 0 – 10 years, 32.0% (12 banks) have been in operation between for periods between 11 – 20 years, while 10% (4 banks) have been in operation for 20 years and above. This indicates that majority of the banks have not been in operation for more than a decade and their macroeconomic experience in the financial sector is in cycles of five years.

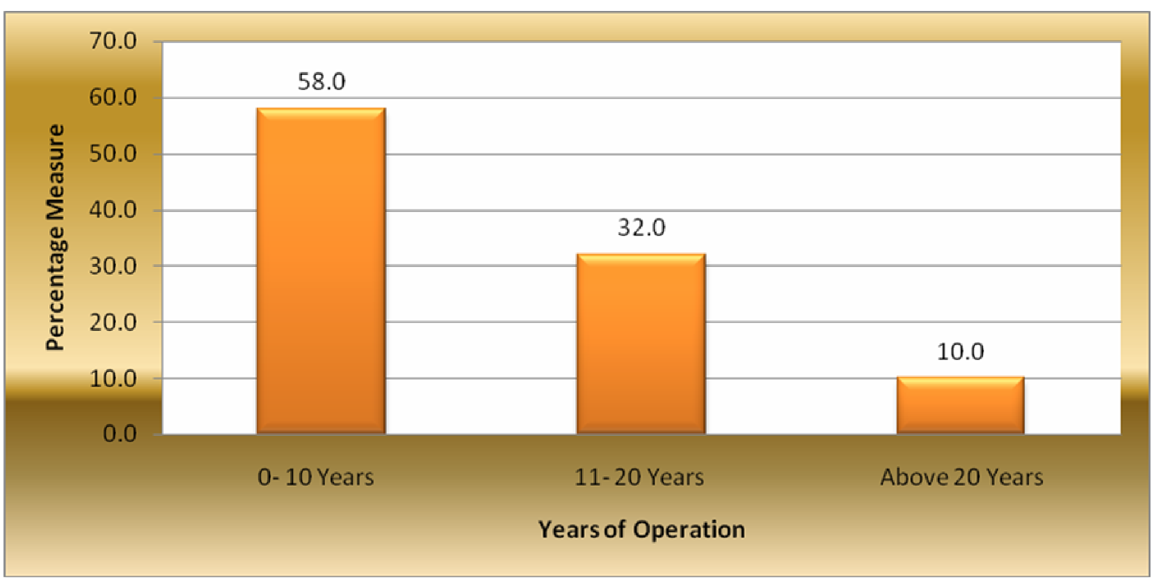

Figure 4.4: Years of Operation

4.2.3 Ownership Structure

The study was able to enumerate the ownership in terms of shareholding structure as indicated in table 4.1 below.

Banks	Ownership
1. ABC Bank (Kenya)	Private bank with few shareholders
2. Bank of Africa	Private bank with few shareholders
3. Bank of Baroda	Private bank with many shareholders
4. Bank of India	Private bank with many shareholders
5. Barclays Bank	Private bank with many shareholders
6. CFC-Stanbic Bank	Private bank with few shareholders
7. Chase Bank	Private bank with few shareholders
8. Citibank	Private bank with few shareholders
9. City Finance Bank	Private bank with few shareholders
10. Co-operative Bank of Kenya	SACCO in Kenya
11. Commercial Bank of Africa	Private bank with few shareholders
12. Consolidated Bank of Kenya	State-owned bank
13. Credit Bank	Private bank with few shareholders
14. Development Bank of Kenya	Private bank with few shareholders
15. Diamond Trust Bank	Private bank with few shareholders
16. Dubai Bank	Private bank with many shareholders
17. Ecobank	Private bank with few shareholders
18. Equatorial Commercial Bank	Private bank with few shareholders
19. Equity Bank	Private bank with many shareholders
20. Family Bank	Private bank with few shareholders
21. Fidelity Commercial Bank	Private bank with few shareholders
22. Fina Bank	Private bank with few shareholders
23. First Community Bank	Private bank with few shareholders
24. Giro Commercial Bank	Private bank with few shareholders
25. Guardian Bank	Private bank with few shareholders
26. Gulf African Bank	Private bank with few shareholders
27. Habib Bank A.G Zurich	Private bank with few shareholders
28. Habib Bank	Private bank with few shareholders
29. Housing Finance	Private bank with few shareholders
30. Imperial Bank	Private bank with few shareholders
31. Investment & Mortgages Bank	Private bank with few shareholders
32. Kenya Commercial Bank	State-owned bank with many private shareholder
33. K-Rep Bank	Private bank with few shareholders
34. Middle East Bank	Private bank with few shareholders

35. National Bank of Kenya	Private bank with few shareholders
36. NIC Bank	Private bank with few shareholders
37. Oriental Commercial Bank	Private bank with few shareholders
38. Paramount Universal Bank	Private bank with few shareholders
39. Prime Bank	Private bank with few shareholders
40. Southern Credit Banking Corp.	Private bank with few shareholders
41. Standard Chartered Bank	Private bank with few shareholders
42. Trans-National Bank	Private bank with few shareholders
43. United Bank for Africa	Private bank with few shareholders
44. Victoria Commercial Bank	Private bank with few shareholders

Table 4.1: Ownership Structure Source: CBK, (2009)

4.2.4 Product Range

During the year 2009, banks continued to introduce new products that comprised mainly of new deposit accounts and electronic banking products leveraging on mobile phone technology. Table 4.2 gives a summary of a cross sectional assessment of Kenyan bank products and services provided.

Product	**Customer Percentage Utility**
Ordinary Account	100%
Current Accounts	93%
Savings Accounts	86%
Business Account	45%
Corporate e-Banking	59%
Cash Back Services	78%
Internet Banking services	68%
SMS Banking	67%
Loans	100%
Swift Codes	23%
Mobile Banking	39%
ATM Services	100%
Documentary Collections/Bills for Collection	12%

SME Banking	30%
Money Transfer	83%
Custodian Services	26%
Business Advisory Services	10%
Credit Cards	58%
Debit Cards	33%
Investment Financing	65%
Direct Financing	63%
Insurance Services	9%
Stock Share Trading	8%

Table 4.2 Product Range Sources: CBK, (2009)

4.3 Objective of the Study

The objective of the study was to establish the relationship between competitive strategies and performance of commercial banks in Kenya.

4.3.1 Competitive Strategies

The study used descriptive statistics in the form of arithmetic mean and standard deviation and computed for multiple dimensions that have been assessed through the questionnaires as presented in the subsequent tables. Frequency distribution was also used to show the percentage of observations falling into each of several ranges of values. Frequency distributions are portrayed as histograms.

4.3.1.1 Low Cost Leadership Strategy

For low-cost leadership strategy, the responses indicated that majority of the banks have adopted cost cutting techniques as a competitive strategy, having the highest mean of 3.41 with a standard deviation of .547, followed by maximization of economies of scale with a mean of 3.24 and a standard deviation of .538. Avoiding loss-making areas came third with a mean of 3.12 and standard deviation of .510. Finally, under this category improved process efficiencies came last with a mean of 3.00 and standard deviation of .592.

Variables		Mean	Standard Deviation
1	Improved process efficiencies	3.00	.592
2	Maximized economies of scale	3.24	.538
3	Implemented cost cutting techniques	3.41	.547
4	Avoided loss-making areas	3.12	.510

Table 4.3 Low Cost Leadership Strategy

Figure 4.5 below assesses the low cost leadership strategy utility by the respondent banks. The majority of the banks adopted cost cutting techniques indexed by 36%, followed by economies of scale at 29%, thirdly avoidance of loss making areas recorded 23% and finally improved process efficiency received the lowest rating of 12%.

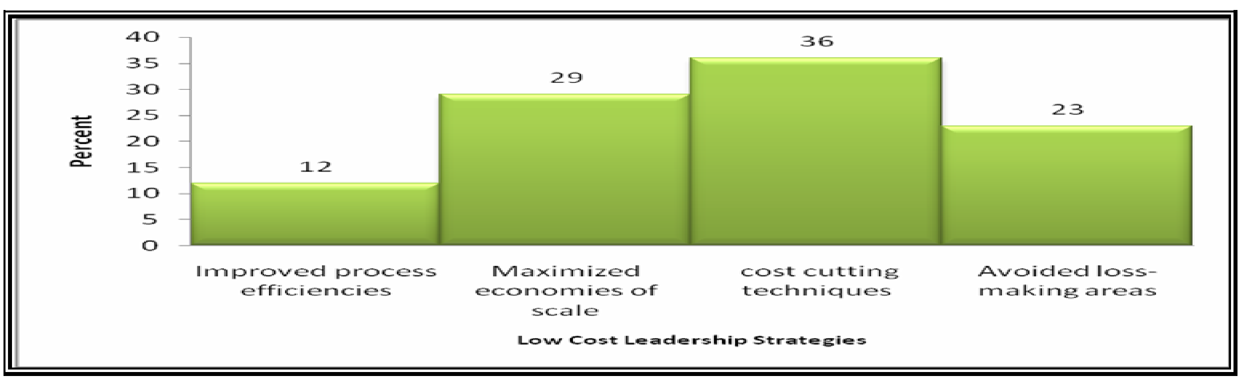

Figure 4.5: Low Cost Leadership Strategy

4.3.1.2 Differentiation Strategy

Assessing the differentiation strategy, the responses indicated that a majority of the banks have introduced unique features to existing products and services as a competitive strategy, having the highest mean of 3.05 with a standard deviation of .669, followed by the introduction of unique products at a mean of 2.85 and a standard deviation of .573. Product differentiation through service network that supports these products and services came third with a mean of 2.76 and standard deviation of .663. Marketing channels through which these products and services are delivered came last under this category with a mean of 2.73 and standard deviation of .742.

Variables		**Mean**	**Standard Deviation**
1	Improved or introduced unique features to existing products and services	3.05	.669
2	Introduced new unique products and services	2.85	.573
3	Marketed channels through which these products and services are delivered	2.73	.742
4	Improved the service network that supports these products and services	2.76	.663

Table 4.4: Differentiation Strategy

Figure 4.6 evaluates frequency distribution of differentiation strategies adopted by the commercial banks. Under this category, improved or introduction of unique features to existing products and services indexed the highest rating at 46%, followed by Improvement of the service network that supports these products and services at 23%. Introduction of new unique products and services indexed 21% and finally marketed channels through which these products and services are delivered indexed 10%.

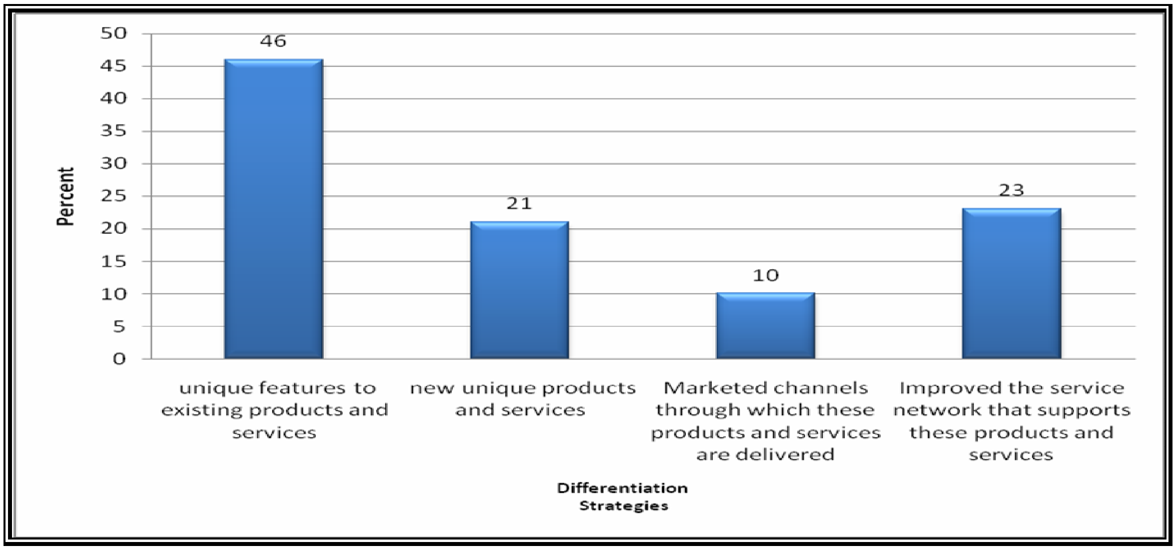

Figure 4.6: Differentiation Strategy

4.3.1.3 Focus Strategy

On the count of focus strategy, the responses indicated that Focusing on a specific niche / segment in the market and Offering specialized products and services to that niche / market segment are key competitive strategy recording a mean and a standard deviation of 3.05, 2.85 and .699 and .524 respectively. Expanding branch networks to isolated geographical areas and tailoring products and services to the demands of the small-to-medium sized customers received an equal mean of 2.54 in terms of importance as competitive strategy and a standard deviation of .711 and .636 respectively.

Variables		**Mean**	**Standard Deviation**
1	Focused on a specific niche / segment in the market	2.95	.669
2	Offered specialized products and services to that niche / market segment	3.02	.524
3	Expanded branch networks to isolated geographical areas	2.54	.711
4	Tailored products and services to the demands of the small-to-medium sized customers	2.54	.636

Table 4.5: Focus Strategy

Figure 4.7 examines the banks focus strategies under different categories. Focus on a specific niche / segment in the market registered a 53% response rate. The second leading score was the offer of specialized products and services to that niche / market segment at 27%. Finally both categories of expanded branch networks to isolated geographical areas and tailored products and services to the demands of the small-to-medium sized customers indexed 10% each.

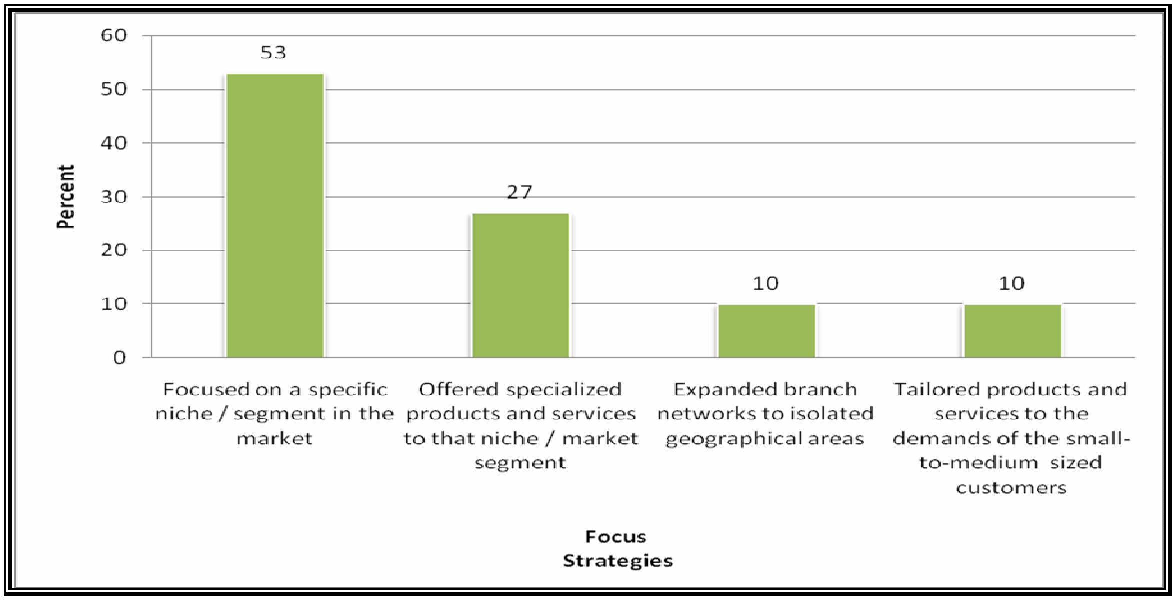

Figure 4.7: Focus Strategy

4.3.2 Firm Performance

Findings on performance data was collected from the financial statements of banking institutions operating in Kenya as well as from the Central Bank of Kenya's website. These secondary data was captured through the Performance Capture Forms (See Appendix III). The main performance measures featured were: Profitability (as measured by return on assets and return on equity); Capital and Risk Weighted Assets (as measured by core capital to risk weighted assets ratio and total capital to risk weighted assets ratio); and Market Share (as measured by total net assets, net advances, deposits, capital & reserves and profit).

4.3.3 Relationship between Competitive Strategies and Firm Performance

4.3.3.1 Correlation Analysis of Competitive Strategies and Firm Performance

Correlation analysis tests for the interdependence of the variables. It makes no assumption as to whether one variable is dependent on the other(s) and is not concerned with the relationship between variables; instead it gives an estimate as to the degree of association between the variables.

The Pearson's product-moment correlation coefficient was used to give an estimate as to the degree of association between the variables. This technique was opted for because the data used in the study is interval/ ratio-type kind of data (not ordinal data). Pearson's correlation coefficient assumes that each pair of variables is bivariate normal and it is a measure of linear association.

Variables used were arranged in a matrix such that where their columns/rows intersected there were numbers telling about the statistical interaction between the variables. Three pieces of information were provided in each cell: the Pearson correlation, the significance, and number of cases.

The tables below illustrate the findings of the measures of the degree of association between the various competitive strategies and profitability:

Table 4.6 Correlation between Competitive Strategies and Return on Asset

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.423	1		
3. Focus Strategy	.078	.165	1	
4. Return on Asset	.678**	.687**	.522**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between return on assets and the respective competitive strategies. Correlations in table 4.6 demonstrate that competitive strategies have a strong significant positive relationship with banks' return on assets indicating that the three competitive strategies influence firm performance to a greater extent.

Table 4.7 Correlation between Competitive Strategies and Return on Equity

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.134	1		
3. Focus Strategy	.567	.453	1	
4. Return on Equity	.543**	.576**	.786**	1

Notes: ** represent correlation is significant at 0.01 levels (2 –tailed)

The study measured the relationship between return on equity and the respective competitive strategies. The results presented in table 4.7 indicate that return on equity correlates significantly with the competitive strategies. This strong positive relationship influences firm performance to a large extent as the strategies are pursued in different dimensions.

Table 4.8 Correlation between Competitive Strategies and Core Capital to Risk Weighted Assets

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.063	1		
3. Focus Strategy	.031	.129	1	
4. Core Capital to Risk Weighted Assets	.313**	.210**	.255**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between core capital to risk and the respective competitive strategies Table 4.8 shows that there is statistically a weak positive relationship between all the variables indicating that the competitive strategies affect a firm's performance but with less magnitude as far as core capital to risk weighted assets are concerned.

Table 4.9 Correlation between Competitive Strategies and Total Capital to Risk Weighted Assets

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.227	1		
3. Focus Strategy	.542	.076	1	
4. Total Capital to Risk Weighted Assets	.395**	.323**	.377**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between total capital to risk and the respective competitive strategies .There was also a statistically weak positive relationship between all the variables in Table 4.9 establishing that the competitive strategies affect firm's performance but with less magnitude as far as total capital to risk weighted assets are concerned.

Table 4.10 Correlation between Competitive Strategies and Net Assets

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.258	1		
3. Focus Strategy	.398	.347	1	
4. Net Assets	.414**	.465**	.427**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between net assets and the respective competitive strategies here was a fairly strong positive significant relationship between net assets of the banks and the competitive strategies as indicated in Table 4.10.

Table 4.11 Correlation between Competitive Strategies and Net Advances

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.212	1		
3. Focus Strategy	.142	.160	1	
4. Net Advances	.318**	.310**	.354**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between return on net advances and the respective competitive strategies. There was a relatively weak positive correlation between net advances and the competitive strategies under assessment as indicated in table 4.11.

Table 4.12 Correlation between Competitive Strategies and Deposits

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.111	1		
3. Focus Strategy	.268	.340	1	
4. Deposits	.510**	.517**	.599**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between deposits and the respective competitive strategies. There was a significant strong positive relationship between deposits and the competitive strategies, as illustrated in Table 4.12. This supports that competitive strategies are significant in explaining the variance in firms' performance over time.

Table 4.13 Correlation between Competitive Strategies and Capital & Reserves

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	. 243	1		
3. Focus Strategy	.013	.176	1	
4. Capital & Reserves	.334**	.367**	.326**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between return on equity and the respective competitive strategies. The results presented in table 4.13 indicate that capital and reserve relate less significantly with the competitive strategies. This positive relationship influences firm performance to an extent as the strategies are pursued in different dimensions.

Table 4.14 Correlation between Competitive Strategies and Profits

	1	2	3	4
1.Low-Cost Leadership Strategy	1			
2. Differentiation Strategy	.523	1		
3. Focus Strategy	.123	.190	1	
4. Profits	.891**	.734**	.720**	1

Notes: ** represent correlation is significant at 0.01 level (2 –tailed)

The study measured the relationship between profits and the respective competitive strategies .Table 4.14 shows that there is statistically strong positive relationship between all the variables. The competitive strategies affect firm's performance with a significant magnitude as far as banks overall profits is concerned.

4.3.3.2 Regression Analysis of Competitive Strategies and Firm Performance

Regression analysis involves identifying the relationship between a dependent variable and one or more independent variables. Multivariate analysis was used to evaluate the simultaneous effects of all the independent variables on the dependent variable.

A model of the relationship was hypothesized, and estimates of the parameter values used to develop an estimated regression equation. Various tests were then employed to determine if the model was satisfactory. If the model was satisfactory and the estimated regression equation was used to predict the value of the dependent variable given values for the independent variables.

The results of regression of the three independent variables against the dependent variable i.e. firm performance are shown in table 4.15.

Table 4.15 Aggregate Impact of Competitive Strategies on Firm Performance

R	R^2	Adjusted R^2	Std. error of the estimate	F	Sig. F
0.615	0.378	0.319	2.676	6.388	0.0005

The square of the multiple R is 0.378 indicating that the 37.8% of the variance in firm performance is explained by the three competitive strategies jointly. The F value is 6.388 that is significant at P = 0.0005 suggesting that the three independent variables have significantly explained 37.8 percent of the variance in the firm performance.

The strength of influence that each of the independent variable had on the dependent variable was determined by the use of multiple regression coefficient of the independent variables. The influence of each independent variable is shown in Table 4.14.

Table 4.16 Influence of Independent Variables on Firms Performance

Variable	Std. error	Standard beta	t	Significance
Low-Cost Leadership Strategy	0.051	0.389	2.360	**0.021**
Differentiation Strategy	0.102	0.266	2.218	**0.030**
Focus Strategy	0.079	0.139	0.1202	**0.023**
Constant	**0.051**	**1.005**	**2.935**	

As shown in table above low-cost leadership strategy had the strongest significant influence on firm performance with a standardized beta of 0.389. Indicating that for a unit increase in this strategy, an organization is likely to improve its performance by 39 percent. Differentiation strategy had a significant effect of 0.266 while focus strategy had 0.139.

Table 4.14 shows the influence of the variables which are included in the regression. Consequently, the final equation of the multiple regression is:

Y = 1.005 + 0.389 *Low-Cost Leadership Strategy* + 0.266 *Differentiation Strategy* + 0.139 *Focus Strategy*

Where: Y = Firm Performance.

4.4 Discussion of Findings

Those interviewed predicted a sustained level of performance through continuous implementation of competitive strategies. Competitive strategies have enabled these banks to proactively evaluate future challenges in the banking industry. It should be however noted that though the above competitive strategies were indicated to be very significant, there were different degrees of variation among respondents with respect to the extent to which sources were significant. This is as indicated by the standard deviation of each of the competitive strategies.

Theory has shown that competitive methods used by banks conform to generic strategy types. Banks following a cost leadership strategy realize statistically significant superior performance compared to those that are stuck-in-the-middle. Banks that pursue broad differentiation, customer service differentiation and focus strategy report above average returns.

The study indicates that larger return to equity and return to asset ratios lead to more profit margins with well calculated competitive strategies. This finding is intuitive and consistent with previous studies. The study's findings also indicated that some competitive strategies have a weaker role on the capital ratios of commercial banks in Kenya and in addition the findings suggested that competitive strategies have less impact on bank reserves.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter summarizes the findings and makes conclusions based on the objective of this study which is to establish the relationship between competitive strategies and the performance of commercial banks in Kenya. This chapter also includes the recommendations for improvements, the limitations of the study as well as the recommendations for further research.

5.2 Summary

The overall results indicated that majority of these banks have 11 – 20 branches country wide, have been in operation for periods of less than 10 years, have a staff count of less than 1,500 employees and with their focus on the East African region.

Findings from this study showed that low-cost leadership strategy as an independent variable recorded the highest mean of 3.19 with standard deviation of 0.547. Differentiation strategy was second with a mean of 2.85 and standard deviation of 0.662, and finally, Focus strategy was least recording a mean of 2.76 with standard deviation of 0.643.

The study also established that correlation between competitive strategies and firm performance indicators that recorded a significant strong positive relationship were return on assets, return on equity, deposits and firm profits. The following firm performance indicators had a weak positive relationship with the devised competitive strategies in the study i.e. total capital to risk weighted assets, net assets, capital & reserves and core capital to risk weighted assets.

The strength of influence that each of the independent variable had on the dependent variable was determined by the use of multiple regression coefficient of the independent variables whose results show that low-cost leadership strategy had the strongest significant influence on firm performance with a standardized beta of 0.389. Indicating that for a unit increase in this strategy, an organization is likely to improve its performance by 39 percent. Differentiation strategy had a significant effect of 0.266 while focus strategy had 0.139.

5.3 Conclusions

The preceding empirical analysis allows us to shed some light on the relationship between competitive strategies and performance measures in commercial banks in Kenya. Competitive methods used by commercial banks conform to generic strategy types. Commercial banks have employed different strategies to remain competitive in the industry. It should be noted that competitive strategies adopted by commercial banks provided different degrees of variation among the respondents with respect to which competitive strategy was adopted. This is evidenced by the standard deviation of each of the strategies.

From the summary of the findings, the commercial banks profitability measures respond more positively to the increases in competitive strategies that are cost driven as opposed to product and focus frameworks. Commercial banks following a cost leadership strategy realized statistically significant superior performance as compared to those that pursued broad differentiation, customer service differentiation and focus strategy that reported above average returns.

The results revealed that larger return to equity and return to asset ratios lead to more profit margins with well calculated competitive strategies. This finding is intuitive and consistent with previous studies. The study's findings also indicated that some competitive strategies have a weaker role on the capital ratios of commercial banks in Kenya and in addition the findings suggested that competitive strategies have a less impact on bank reserves.

In examining the relationship between competitive strategy variables and the performance of commercial banks, the results confirm the predictions of the banks performance. The evidence therefore suggests that adopted competitive strategies by commercial banks are important in terms of determining profitability and enhanced performance. One can therefore conclude from the results, that the competitive strategies are relevant in the context of commercial banks' performance.

5.4 Recommendations

From the discussions and conclusions in this chapter, the researcher recommends that although there are some challenges in implementing the competitive strategies in the banking sector, such as increased number of competitors, competitive strategies are very important for the banks to remain competitive in the market.

In the banking industry, understanding the market structure is a key determinant of the successful implementation of a cost leadership, differentiation or focus strategy. For instance, differentiating banking services, responsive customer service, rapid product innovations, branding, service quality and relationship banking are areas where financial institutions may pursue differentiation strategies. However, the differentiation strategy may be difficult to implant in a service industry since services are easily copied and fruitful options may be limited due to the simplicity and imitability of financial services, unless the target market is highly sophisticated and knowledgeable.

The researcher highly recommends that commercial banks consider shifting more of their focus to the cost leadership strategy. Mass production, mass distribution, economies of scale, technical & product design, input cost and capacity utilization of resources are areas where the cost leadership strategy can be pursued. For instance, banking institutions have labored to retain core deposits on the realization that deposits grow in direct proportion to customer satisfaction. To ensure success in this, commercial banks should consider offering their products to customers at minimal or even zero costs and scrap off the minimum balance requirement to open or to run an account. This would consequently lead to drawing of substantial deposit amounts.

Commercial Banks with weak return on asset (ROA) and return on equity (ROE) should further strengthen their position of cost leadership by improving their process efficiencies, maximizing economies of scale, implementing cost-cutting techniques and avoiding loss-making areas to achieve cost leadership. In order for banks to adopt cost leadership strategy, they must increase their competitive ability via achieving ratios of return for the stockholders and the depositors that are higher than the current ones.

Banks should also be able to deliver the same products / benefits as competitors but at a lower cost (cost advantage) or deliver benefits that exceed those of competing products (differentiation advantage) to gain a competitive advantage over other firms, for instance commercial banks with low profit margins should develop their current products as well as innovate new financial products in line with the development trends in the industry. In addition, they should navigate in new markets and new products in the finance industry, like establishing or investing in insurance companies, investment companies, or financial security dealer companies.

Commercial banks should focus on customer- oriented strategies instead of a product oriented ones. The contemporary trend in banks' marketing focuses essentially on the customer, the availability of a wide range of banking services is not sufficient on its own. For example, the banking customers are sensitive to both loan & deposit rates therefore the banks following a cost leadership strategy may realize a performance advantage over those that pursue differentiation or focus strategy.

5.5 Limitations of the Study

Due to tight schedules, some interviewees took a lot of time to make their responses. This prompted the researcher to do a lot of follow up with the respondents to ensure that feedback was given within the allotted time.

Some respondents were skeptical about the intentions of the researcher. Some managers were unwilling to divulge information that they deemed secretive and this led to some incomplete information from these respondents.

5.6 Suggestions for Further Research

This study recommends for further research to be conducted on other dimensions of competitive strategies, for instance to determine how external and /or internal environmental factors have influenced the implementation of competitive strategies & thus performance of commercial banks in Kenya.

Further research should also be conducted to establish the factors that influence the choice of competitive strategies adopted by the commercial banks in Kenya. This will assist the bank's management to understand the key areas on which to lay emphasis on.

Since this study adopted a census research design and it was not possible for all the banks to participate in the research, a case by case study would assist in bringing out some unique findings about specific banks. This will increase the chances for capturing data that was not captured during this study.

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APPENDICES

APPENDIX I: QUESTIONNAIRE

Dear Respondent,

My name is Gladys Wanjiku Kamau, a final year MBA student at the University of Nairobi. I am required to carry out a research in my area of study as part of the course requirements. In this regard, my research is to explore the relationship between competitive strategies and the performance of commercial banks in Kenya. The information that you will give will be used purely and solely for academic purposes and will be treated with utmost confidentiality. Your cooperation will be highly appreciated.

Part A: Organizational Bio- data

1. Name of your bank ____________________________

2. Size of the bank (Tick as appropriate)

a. 2 to 10 branches [ ]

b. Between 11 to 20 branches [ ]

c. Above 20 branches [ ]

3. Year of incorporation ____________________________

a. Less than 10 years ago [ ]

b. Between 11 to 20 years ago [ ]

c. Over 20 years ago [ ]

4. Size of the bank in terms of number of employees (Tick as appropriate)

a. Below 1,500 [ ]

b. Between 1,501 to 3,000 [ ]

c. Between 3,001 to 6,000 [ ]

d. Over 6,001 [ ]

5. Scope of operations (Tick as appropriate)

a. Local (Within Kenya) [ ]

b. Regional (Within East Africa) [ ]

c. Global (Africa & beyond) [ ]

Part B: Adoption of Competitive Strategies

These questions intend to measure the extent of the adoption of selected competitive strategies i.e. low-cost leadership, differentiation and focus.

Use the Key below to tick as appropriate.

[1] – NOT AT ALL; [2] – TO A LESS EXTENT; [3] – TO A MODERATE EXTENT; [4] – TO A LARGE EXTENT; [5] – TO A VERY LARGE EXTENT.

To what extent has your bank adopted the following strategies as a competitive strategy?

6. Low-Cost Leadership Strategy:

i.	Improved process efficiencies?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
ii.	Maximized economies of scale?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
iii.	Implemented cost cutting techniques?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
iv.	Avoided loss-making areas?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**

7. Differentiation Strategy:

i.	Improved or introduced unique features to existing products and services?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
ii.	Introduced new unique products and services?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
iii.	Marketed channels through which these products and services are delivered?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
iv.	Improved the service network that supports these products and services?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**

8. Focus Strategy:

i.	Focused on a specific niche / segment in the market?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
ii.	Offered specialized products and services to that niche / market segment?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
iii.	Expanded branch networks to isolated geographical areas?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**
iv.	Tailored products and services to the demands of the small-to-medium sized customers?	**[1]**	**[2]**	**[3]**	**[4]**	**[5]**

General View

9. What recommendation can you suggest to management to enhance your bank's competitive strategies?

____

____

____

____

____

____

10. Please provide any other information that you consider important for this study.

____

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____

Thank you for your cooperation.

APPENDIX II: LIST OF COMMERCIAL BANKS IN KENYA

1. ABC Bank (Kenya)
2. Bank of Africa
3. Bank of Baroda
4. Bank of India
5. Barclays Bank
6. CFC-Stanbic Bank
7. Chase Bank
8. Citibank
9. City Finance Bank
10. Co-operative Bank of Kenya
11. Commercial Bank of Africa
12. Consolidated Bank of Kenya
13. Credit Bank
14. Development Bank of Kenya
15. Diamond Trust Bank
16. Dubai Bank
17. Ecobank
18. Equatorial Commercial Bank
19. Equity Bank
20. Family Bank
21. Fidelity Commercial Bank
22. Fina Bank
23. First Community Bank
24. Giro Commercial Bank
25. Guardian Bank
26. Gulf African Bank
27. Habib Bank A.G Zurich
28. Habib Bank
29. Housing Finance

30. Imperial Bank
31. Investment & Mortgages Bank
32. Kenya Commercial Bank
33. K-Rep Bank
34. Middle East Bank
35. National Bank of Kenya
36. NIC Bank
37. Oriental Commercial Bank
38. Paramount Universal Bank
39. Prime Bank
40. Southern Credit Banking Corporation
41. Standard Chartered Bank
42. Trans-National Bank
43. United Bank for Africa
44. Victoria Commercial Bank

Source: Central Bank of Kenya, (2009).

APPENDIX III: PERFORMANCE CAPTURE FORMS

The performance capture forms are designed to cover the following information:

Profitability of Banking Sector as at December 2009

a) RETURN ON ASSETS (ROA)

	TOTAL ASSETS & CONTINGENCIES					**RETURN ON ASSETS (ROA) %**				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	-	-	-	-	-	-	-	-	-	-

b) RETURN ON EQUITY (ROE)

	SHAREHOLDERS' EQUITY					**RETURN ON EQUITY (ROE) %**				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	-	-	-	-	-	-	-	-	-	-

Capital and Risk Weighted Assets as at December 2009

a) CORE CAPITAL TO RISK WEIGHTED ASSETS RATIO

	CORE CAPITAL (Kshs '000)					**CORE CAPITAL TO RISK WEIGHTED ASSETS RATIO**				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	-	-	-	-	-	-	-	-	-	-

b) TOTAL CAPITAL TO RISK WEIGHTED ASSETS RATIO

	TOTAL CAPITAL (Kshs '000)					**TOTAL CAPITAL TO RISK WEIGHTED ASSETS RATIO**				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	-	-	-	-	-	-	-	-	-	-

Market Share as at December 2009

a) TOTAL NET ASSETS

	TOTAL NET ASSETS (Kshs. Million)					MARKET SHARE %				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**

b) NET ADVANCES

	NET ADVANCES (Kshs. Million)					MARKET SHARE %				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**

c) DEPOSITS

	DEPOSITS (Kshs Million)					MARKET SHARE %				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**

d) CAPITAL & RESERVES

	CAPITAL & RESERVES (Kshs. Million)					MARKET SHARE %				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**

e) PROFIT

	PRE-TAX PROFITS (Kshs. Million)					MARKET SHARE %				
Banks	**2009**	**2008**	**2007**	**2006**	**2005**	**2009**	**2008**	**2007**	**2006**	**2005**
-	-	-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-	-	-
GRAND TOTAL	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**