STRATEGIC RESPONSES TO ENVIRONMENTAL CHALLENGES FACING FAULU BANK IN KENYA

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DECLARATION

This research project is my original work and has never been submitted for examination to any other University.

Signature…………………………….. Date………………………………

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D61/70984/2014

This project has been submitted with my authority as the university supervisor.

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DEDICATION

This project is dedicated to my parents Mr. and Mrs. Kamwere, my brothers Kelvin Charchi Kamwere and Anthony Nderitu Kamwere, my Aunt Mary Waithiegeni Githinji, my Uncle Ephantus Maina Githinji and my grandmother Beatrice Wangui Githinji for their moral support and encouragement when I was pursuing my studies.

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ABBREVIATIONS AND ACRONYMS

AMFI	Association of Microfinance institutions
CBK	Central Bank of Kenya
MFIs	Microfinance Institutions
NGO	Nongovernmental Organization
PESTEL	Political, Economic, Social, and Technological
RBV	Resource-based View

ABSTRACT

Organizations face various challenges that emanate from the environment that forces firms to adopt strategies to deal with this kind of challenges to counter competition. This study intended to determine the environmental challenges affecting Faulu bank and to identify the strategic responses adopted by Faulu bank to cope with the environmental challenges. The study used a case study research design; primary data was collected with the help of an interview guide. A face-to-face interview was carried out by interviewing four departmental heads at Faulu bank. These departments included marketing department, finance department, operations department and research and development department. Data was analyzed using content analysis which is a systematic and qualitative description of the composition of the objects of the study. The study found that the environmental challenges that faced Faulu bank were competition, obsolete technology, evolving customer needs, complying with regulatory requirements and political instability. It was observed that these challenges hindered Faulu bank's survival in environment and thus necessitated the bank to find strategies to deal with the situation. It was further concluded that the main strategic responses adopted by Faulu bank to deal with environmental challenges included the adoption of product and service innovation, use of modern technologies, product differentiation, investing in research and development programmes, strategic talent management programme and training and development programme. The study recommends that Faulu bank should increase its budgetary allocation on research and development to enhance innovation in the existing products to allow firms to develop new products and adopt better approaches to produce quality products and services. Further, Faulu Bank should invest more on information communication technology to achieve system integration this will increase sharing of information and communication in the bank hence boost efficiency in banking operations and decision making. The study was limited to Faulu bank and hence the findings obtained in this study are unique and cannot therefore be used for direct application in any other Microfinance bank to make generalization. Future researchers should conduct a similar study in all the Microfinance banks in Kenya or the baking industry in Kenya. The findings obtained can then be used to make comparison and a conclusion can be drawn based on facts.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The world of business is constantly altering the environment is uncertain and customer needs keep on changing. Threat of competition also poses a major risk for sustainability and competitiveness. Pearce & Robinson (2007) argue that to deal with environmental challenges organizations have opted to adopt strategic responses as a component to counter changes in the environment in order to realize their vision and mission. Apparently organizations are conducting a careful analysis that is considered necessary in identifying appropriate strategies ones that will assist in the realization of the set goals and objectives while striving to minimize any possible negative effects. According to Thompson & Strickland (2002) to respond to changes in the external environment organizations have to craft strategies that are responsive to environmental regulations.

This study is informed by three theories namely Open-Systems Theory, Resource-Based View and Resource Dependence Theory. In open-systems theory the external control of the firm relies on the notion that an organization's choices of behaviour and actions are examined by scanning the environment in which the organization operates. The Resource-Based View (RBV) is based on the premise that an organization's internal environment on the basis of its resources and capabilities are more significant in the determination of the strategic action rather than the external environment (Barney, 2001). Resource dependency theory is based on the premise that resources are essential to organizational success and that access and control over resources is a basis of power (Lamb & Boyden, 2011).

In Kenya banks respond in different ways to changes in the environment the most common response strategies used globally are mergers and acquisitions strategic alliances and product differentiation and product innovation. The banking industry is not an exception to environment uncertainty. This has been brought about by stiff competition and adoption of banking technologies. Faulu bank is one of the microfinance banks that should consider adopting strategic responses to achieve flexibility efficiency and product differentiation (Kamanja, 2015).

1.1.1 Environmental Challenges

Environment challenges include all those actions or situations that have either a positive or a negative effect on a business operations. These situations or actions can either have a positive or a negative effect on the business. Environmental challenges in this study will involve factors that take place outside the organization and are difficult to predict and control. Beckman, Haunschild and Phillips (2004) maintain that external factors are more dangerous for the organization since they are unpredictable. These factors are Political Economic Social and Technological (PESTEL), factors. This is popularly known as PESTEL. PESTEL Analysis is an instrument that helps in the identification and analysis of the vital drivers of change in the strategic or business environment. Additionally, the tool enables the assessment of the existing environment and potential changes. The internal politics is a key component to consider when analyzing the business environment such as personal interest might affect the kind of strategic response adopted by an organization. The external politics refer to factors that are outside the control of the organization. These factors are tax policies laws that regulate employment trade restrictions reforms environmental regulations political stability and tariffs. Economic factors consider all the events that have an effect on the internal and external economic environment.

Internal factors related to the viability of the strategic responses adopted by the organization. The external events are financial availability to support implementation of the chosen strategic response (Beckman et al., 2004). Castrogiovanni (2002) explains that social factors are important to consider in a business that operates in an uncertain environment. This includes cultural expectations this entails how the customer and the society might be affected by the adoption of a strategic response regarding the norms career altitudes and global warming among others. Implementation of strategic response must consider the nature of technology that keeps on changing especially on matters concerning entry barriers and changes to financial decisions. The organization should also consider the legal setting of the environment to ensure that the way an organization responds to environmental challenges conforms to the legal requirement in place such as taxation resources and employment. The top management should take into account social or economic ecological and environmental features. These features include factors such as natural calamities environmental conservation among others.

1.1.2 Strategic Responses

Porter (2008) defines a strategic action or a strategic response as a market-based effort that involves a substantial commitment of administrative resources and is difficult to implement and reverse. The significance of strategic responses is that they aid the firm to deal with challenges in the external environment that is beyond the firm’s control. To realize success in adoption of strategic responses the organization should align these responses to organizational goals and objectives. Strategic responses are actions taken by an organization to counter competition and remain relevant in the market.

There are two types of strategic responses that guide the kind of decisions made by the organization. These responses can either be strategic or operational in nature (Proff, 2000).There are two types of responses adopted by organizations namely operational and strategic responses. Strategic responses influence two levels of the organization, corporate and business levels. Strategic responses are meant to enable the firm to position itself competitively against its competitors and to meet customer demands and expectations. Porter (2008) argues that the kind of strategies adopted by the firm has an influence on the firm's survival in the environment hence the top management should select a strategic response that matches the strategic goals. The top management should consider its implications both in the short-run and long-run. Mintzberg (2004) contends that the relevance of a strategic response is to combat competitive pressures from the environment and securing a strategic position in the market.

The management should design a plan on how to ensure that the manner in which an organization responds to market challenges is integrated to organizational goals and objectives. Operational strategies have short-term effects on the organization. Operational responses are intended to assist the organization to run its operations smoothly and to boost its efficiency and effectiveness in achieving strategic goals and objectives of the firm (Pearce & Robinson, 2007). Johnson and Scholes (2000) organizations respond differently to environmental challenges with a view of dealing with competition. Some of the strategic responses that have been adopted globally by firms are strategic alliances, mergers and acquisitions, diversification, product innovation and product differentiation.

1.1.3 Microfinance Banks in Kenya

Microfinance Act of 2006 stipulate the supervisory and regulatory framework for microfinance banks in Kenya. The Microfinance Act was enacted on 2nd of May 2008. The core functions of this Act were licensing supervision and to regulate establishment. This Act allows microfinance banks to mobilize customer deposits from the public. This enables the microfinance banks to lend money and benefit from interest rate which is one of its main sources of income (McIntosh, De Janvry & Sadoulet, 2005). Through an Act of Parliament Microfinance Act (2006) was amended by deleting the term institution and substituting it with Microfinance bank licensed under this act. Microfinance bank is a company which is licensed to carry on microfinance bank business and includes all branches marketing units outlets offices and any other place of business that may receive licensing from the Central Bank of Kenya.

The Association of Microfinance Institutions (AMFI), which was registered in 1999 under the Societies Act by the leading MFIs in Kenya, is a member-based institution that strives to better the Kenyan microfinance industry by building its capacity. This institution was established because of the need for Microfinance Institutions (MFIs) to have a shared voice to lobby government for favorable programs and policies that assist in the sharing of information and experiences and to establish connections with both local and international actors. Currently, there are 12 Microfinance banks that are licensed to work and operate within the confines of the Kenya. They include: Choice Microfinance Bank Limited, Faulu Microfinance Bank Ltd, Kenya Women Microfinance Bank Ltd, SMEP Microfinance Bank Ltd, Remu Microfinance Bank Ltd, Rafiki Microfinance Bank Ltd, Uwezo Microfinance Bank Ltd, Century Microfinance Bank Ltd, Sumac Microfinance Bank Ltd, U&I Microfinance Bank

Ltd, Daraja Microfinance Bank Ltd and Caritas Microfinance Bank Ltd (AMFI, 2016).

Kenya has experienced a tremendous growth of microfinance banks in the last few decades. New microfinance banks have been opened and their number has increased new products adoption of banking technologies and integration has increased access flexibility and availability of banking products and services. Liberalization economic reforms and political stability has created an enabling environment for conducting business. This has however forced microfinance banks to rethink and evaluate their strategies to determine whether it conforms to the market needs and hence forced these banks to find appropriate ways of responding to environmental challenges (Dondo, 2001).

McIntosh et al. (2005) explain that microfinance banks have realized that they need to constantly respond to the changing needs of the customers in order to survive and to effectively compete in the banking environment. Some of the strategic responses commonly used by microfinance banks are as follows product innovation strategic alliances and product differentiation.

1.1.4 Faulu Bank

Faulu bank was started as a development project in 1991. This project was driven by Food for the Hungry International which is a Christian International relief program. The organization was registered as a Non-governmental Organization (NGO) in 1994 whose key objective was to provide credit facilities to low income households and micro-enterprises. Later Faulu expanded to a level that it became self-sufficient (Faulu, 2015). Dondo (2001) explains that in 2000, Faulu bank gained financial stability and its portfolio increased significantly in 2002 after making efforts to enlarge its key target group that was the lower market to accommodate the up-market. Faulu bank faced financial difficulties for 2 years that contributed to a huge loss in 2004 that emanated from a high provision for non-performing loans.

In 2007 Faulu went through a fundamental transformation that made it to become one of the three largest microfinance institutions in Kenya. It consisted of 19 branches, 48 offices with a client base of over seventy six thousands. Its main competitor was Kenya Women Finance Trust that targeted women (Faulu, 2015). On 24th of December 2008 Faulu got an approval letter for a deposit-taking license. Central Bank of Kenya issued the bank with a license on 21st May 2009. By the end of year 2010 Faulu had established a network of 25 branches (CBK, 2015).

Faulu bank has realized the worth of responding to environmental challenges as a way of survival and gaining a competitive advantage against competitors. The bank has recently introduced various banking products and services to widen its market segments, increase access to banking products and serve the needs of customers who were previously underserved. The bank has a business and development department that is actively involved in marketing research to tailor their products and services to meet their diverse needs (Kamanja, 2015).

1.2 Research Problem

Beckman, Haunschild and Phillips (2004) explain that organizations face various challenges that emanate from the environment; these challenges force firms to adopt strategies to deal with this kind of challenges to counter competition. Castrogiovanni (2002) contends that the top management should factor in the turbulent nature of the business environment before arriving at any decision to successfully implement a strategy (Barney, 2001).

The banking sector in Kenya has faced a tremendous growth over the last decade this growth is attributed to banking technologies and product innovation as well as the growth of the middle class. This has forced microfinance banks to find sustainable ways to cope with the market needs. Adoption of strategic responses is one of the ways used by banks to respond to environmental challenges (Dondo, 2001).

Henderson (2013) studied strategic responses utilized by American manufacturing firms to cope with environmental dynamics. It was found that product innovation and product differentiation were the most popular strategic responses used by American manufacturing firms. Scott (2009) investigated strategic responses to environmental challenges adopted by brokerage firms in Europe. It was found that Product innovation, mergers and acquisitions were the key strategic responses used by brokerage firms. Miano (2011) found that environmental changes led to adoption of strategic responses by brokerage firms in Kenya. These responses were product innovation, strategic alliances, product differentiation and mergers and acquisitions. Kilonzi (2012) found that NIC Bank adopted strategic responses to cope with competition. Kawira (2014) found that Old Mutual Holdings adopted strategic responses to cope with environmental challenges such as competition. Little has been done in relation to strategic responses to cope with environmental challenges in the context of microfinance banks especially in Faulu bank.

The study therefore sought to find answers to the following questions: what are the environmental challenges affecting Faulu bank? And what were the strategic responses adopted by Faulu bank to cope with the environmental challenges and what are the environmental challenges?

1.3 Research Objectives

The objectives of the study were

i. To determine the environmental challenges affecting Faulu bank.

ii. To identify the strategic responses adopted by Faulu bank to cope with the environmental challenges.

1.4 Value of the Study

Faulu bank will benefit from the findings of this study since it will learn about the strategic responses adopted by Faulu bank and ways to deal with environmental challenges to achieve sustainability and competitive advantage.

The study will be useful to Central bank of Kenya in formulation of uniform policies for Microfinance banks to engage in fair competition to create a favorable environment for microfinance banks and the entire banking industry to grow and expand.

Academicians and researchers will find the study useful since will it add to the existing body of knowledge. The study will also serve as a point of reference for further research. Other microfinance banks might use the findings for this study in adopting strategic response that contribute to reduced costs and improved quality of products that add value to the customers.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter gives a comprehensive coverage of the literature review that has been discussed in line with the study objectives. It consists of the theoretical foundation for the study and the strategic responses adopted by firms to deal with environmental challenges.

2.2 Theoretical Foundation

This section provides a discussion of the theories that anchor this study. These theories include Open Systems Theory, Resource-based View and Resource Dependency Theory.

2.2.1 Open Systems Theory

Katz and Kahn developed the idea of the open-systems theory in 1966 to expound on the general system theory that arose from the work of ecologists. In “The Social Psychology of Organizations” Katz and Kahn (1978) described closed-system models as models that provide still picture of an organization only pertinent when the company’s environment is stable. However, Katz and Kahn experience confirms that the traditional bureaucratic structures cannot work in the modern dynamic environments.

Katz and Kahn (1978) insist that firms largely reliant on upon their environmental setting for resources such as power and information for instance most banks are competing for customers to increase their sales and boost profitability. However due to competition in the banking industry this is not easy the banks are forced to respond to various challenges in the environment to meet the needs of their customers and achieve competitiveness. As corporations function in a dynamic environment they are forced to act in response to this environment in a way that will stimulate homeostasis and facilitate growth. To adjust to the changes and needs of the environment, an organization has to consume the external forces or obtain control over them.

A basic source of disparity among origins of environments comes from the level of investigation that is chosen. Hatch (1997) described three of the most popular ways of sorting the elements of an organizational environment. The inter-organizational network is well represented by a group of organizations embedded in a compound web of relationships consisting of suppliers', clienteles, competitors, unions, governing agencies and interest groups. To succeed in strategy implementation banks should consider satisfying all the needs of their stakeholders to create a platform for them to effectively respond to various environmental dynamics (McLaughlin & Talbert, 2001).

Corporate agencies hold a vital position because they have legitimate control over activities related with tax regulators and licensing agencies (Pfeffer & Salancik, 2003). Organizational theorists divide the basic environment in favor of analysis into diverse environmental forces or sectors comprising of the social, legal, cultural, political, monetary, technical and physical. The global environment includes features of the environment that cross nationwide boundaries or that are organized over a global scale and affect the concerns of the businesses when it grows beyond the limits of the home nation (Scott, 2002).

2.2.2 Resource-Based View

Resource-Based View (RBV) is based on the concept that the organization is a constituent of a collection of capabilities. Strategic responses enable the organization to accommodate changes in the external environment for purposes of survival. Strategic responses give the organization the capability to counter environmental challenges. These capabilities enable the firm to make maximum use of its available resources (Hoopes, Madsen & Walker, 2003). Barney (2001) explains that resources are inputs into an organization's production process these include capital, employees, skills, finance, equipment, goodwill and gifted managers. Resources are either intangible or tangible in nature. The set for resources available for the firm tends to increase as the firm seeks to enhance its effectiveness and competitiveness. Individual resources might not necessarily lead the firm to a competitive advantage but through synergy and integration of competitive resources (David & Cynthia 1995).

The RBV has been researched extensively in establishing the relationship between the organization's internal characteristics and performance. The basic idea is that the organization is a constituent of different resources put together to enhance competitiveness. The manner in which an organization utilizes its available resources is critical in developing its competitive abilities. This theory holds that the firm's competitiveness is on how best an organization responds to various challenges in the environment. One of the ways used by firms to counter dynamics in the environment is utilization of their core competencies and to develop efficient capabilities that can be valued by their customers. Improving value to customers is one of the main objectives why firms adopt strategic responses in an attempt to tailor their products and services to meet the needs of the consumers.

RBV is a theory that integrates strategic responses and competitiveness. Zott (2003) maintains that RBV puts more emphasis on competitiveness especially maximum utilization of internal resources. Managing a bank's strategic decisions and aligning these strategic responses to firm's vision and mission is critical in enhancing the effectiveness of the adopted strategic responses. This improves efficiency and costs of implementation of strategic responses.

2.2.3 Resource Dependency Theory

Resource Dependence Theory focusses with the way organizational tendencies and patterns are influenced by external asset, for example recyclables. The theory is essential since an organization's aptitude to collect, modify and utilize raw materials faster than competitors can be central to success. RDT is strengthened by the core idea that resources are essential to organizational achievement and that access and govern over resources is a basis of power (Lamb& Boyden, 2011).

Assets are often handled by businesses not in the control over the organization seeking them, which means that strategies must be cautiously considered to sustain open usage to resources. Organizations usually build redundancy into reserve acquisition in order to decrease their reliance on single resources for example by liaising with multiple suppliers (Stern & Stalk, 2001). Resource dependence theory also infers that an organization's strategic options are shaped to a great extent by the environment. Since firms are dependent on the environment for resources they needed to endorse strategies that would permit them to acquire these resources. Therefore, the external environment had already been determined for these businesses and they experienced slight strategic choice.

However those who reinforced the notion of executive choice argued that particular organizations were further effective than others in the similar environments thus proving that planned choice did exist.

In the resource dependency the environment can be considered as the source of rare resources that are critical to a business's existence. The lack of control over these crucial resources gives rise to environmental uncertainty as compared to the lack of information. Environments that comprise high intensities of resources were supposed as less aggressive to the organization's stability whereas those with low levels of resources acted to raise the intensity of competition among firms. Resource dependence theorists argued that in order to reduce the effect of this environmental uncertainty on organizational performance it was necessary for organizations to develop and maintain effective relationships with their exterior environment (Pfeffer & Salami, 2003). According to Ortega (2010) firms that are faced by stiff competition find ways of surviving by trying to gain control over other actors in the environment to minimize the level of dependence on other firms to achieve control over the resources that increase the level of dependence by other firms.

2.3 Strategic Responses to Environmental Challenges

Product innovation is one of the ways that firms use to respond to various challenges in the environment. In the modern world innovation is seen as a tool that enables the organization to gain a competitive edge against its competitors (Geroski, 2008). To counter environmental challenges organizations invest in modern technology such as ICT to improve their efficiency in operations and reduce operational costs. This allows the firms to offer more efficient and flexible services that meet the growing needs of the customers.

Use of modern technologies has enabled firms to achieve integration that easily allows sharing of valuable information with its stakeholders and thus reduced the costs of processing information and supervision (Brass, Galaskiewicz, Greve & Tsai, 2004).

Product innovation is one of the ways that banks use to respond to environmental challenges. Firms that invest in modern technology offer services that are difficult to duplicate by competitors. This has enabled companies to provide cheaper and high-quality services to enhance customer satisfaction. Most banks are utilizing recent technologies to produce products and services that target to address specific needs of the customers such as efficiency flexibility and convenience. Some of the product innovations currently used by commercial banks are use of automated teller machines mobile banking use of debit and credit cards among others. The advantage of product innovation is that it might be difficult for firms to duplicate similar goods and services. Smaller businesses wishing to innovate might be limited to use modern technologies as a result of lack of adequate finances and thus make it difficult for them to innovate products or services (Geroski, 2008).

Mergers and acquisitions is another form of a strategic response used by organizations. Thompson et al., (2008) indicate that combining the operations via merger or acquisition is critical in achieving operating economies increasing the organization's competencies and competitiveness and opening up avenues of new market opportunities. Firms adopt mergers and acquisitions to benefit from reduced costs of operations expansion of geographic coverage expand the organizations business and products portfolio to gain access to modern technologies or other resources for increased competitive advantage.

The benefits of mergers and acquisitions are as follows increase in capital levels a wide distribution network and markets share from the best global practices. The limitation of this strategic response is integrating the divergent corporate cultures on cross-border acquisitions (Thompson & Strickland, 2002).

A strategic alliance is a formal agreement between two or more organizations in which there is strategic collaboration based on a joint contribution of resources, shared risk, shared control and mutual dependence. In most cases strategic alliances consist of joint sales and distribution and joint production (Thompson et al., 2002). The significance of a strategic partnership is that strategic partners can gain competencies and resources from other partners while providing a learning opportunity for their partners. The weakness of strategic alliances is cost, dispute resolution and the possibility that a partner might become a competitor for the other if it gains stability and hence pulls-out of the alliance and decides to operate alone in a similar market segment. Stiff competition has made firms adopt product differentiation as a strategy to counter challenges of competition. This has enabled firms to position themselves competitively in the market to realize competitive advantage against their competitors who are in similar lines of business (Porter, 2008). Scott (2009) notes that downsizing is a kind of a business strategy that is designed to enhance the financial position of a firm by reducing and altering the structure of the employees in order to boost performance. Downsizing is very popular especially in organizations that seek to achieve flexibility, reduce bureaucratic structure, enhance efficiency regarding decision-making, and improve organizational performance. Downsizing is achieved by decreasing the number of employees through layoffs, attrition, redeployment, or early retirement.

Downsizing is reportedly a common response to a developing, global environment. Incorporating downsizing in the strategic management plan can increase organizational efficiency by maintaining a focus on key competencies that promote competitive advantage and increasing or maintaining current market share levels. This leads to organizational performance. Even so, downsizing possesses its own challenges which include decreased morale of the employees who get concerned about who will lose the employment position or not. Downsizing brings along increased costs at the time of paying the arising severance pay (Henderson, 2013).

Thompson (2008) posits that cost leadership means the lowest cost of operation in the industry where the organization producing at the lowest cost in the industry enjoys the best profits. The cost leadership is often driven by company efficiency, size, scale and the length of operation by the organization. A cost leadership strategy aims to exploit scale of production, well defined scope and other economies for example a good purchasing approach, producing homogenous goods and services using high levels of technology is able to offer goods and services at a cheaper cost than its competitors.

Bertone and Clark (2009) posit that producing at lower cost is a strategy that can be used by various firms so as to have significant competitive strategies that can be viable in the long term business environment. Having intelligence of this underlying source of competitive pressure provides the groundwork for strategic agenda of action. A low cost leader's basis for competitive advantage is lower overall costs than competitors. The need to manage costs is challenge to most organizations that struggle to successfully mitigate and control their operating expenses. Successful low cost leaders are exceptionally good at finding ways to drive costs out of their business (Bertone et al., 2009).

Product differentiation is the process of distinguishing a product or a service from others to make it more attractive to a particular target market. In this kind of strategy, the organization provides differentiated goods and services which seek to satisfy the needs of the customers in a more competitive manner. This allows companies to desensitize prices and focus on value that generates a comparatively higher price and a high margin and improved organizational productivity (Mintzberg, 1994). The benefits of differentiation require producers to segment the market in order to target goods and services at specific segments, generating a higher than average price.

Johnson and Scholes (2002) show that an association that separates its items and administrations will cause an extra cost in making their upper hand over contenders. The costs must be balanced by an expansion in income produced by deals. There is a hazard that the separation could be replicated by contenders thus the motivator by associations to dependably enhance and consistently move forward. Focusing on littler market fragments to give unique client needs is a system broadly utilized as a part of the corporate division. It includes distinguishing proof of the requirements of the clients in the market and planning items that can fit their needs. Doorman (2008) argues that, "the non-specific procedure of center lays on the decision of a limited aggressive degree inside an industry. The focuser chooses a section or gathering of portions in the business and tailors its technique to serving them to the prohibition of others. In cost center system, a firm looks for a cost advantage in its objective section (Mintzberg, 2004). Assist, the discoveries uncovered that Faulu bank embraced mergers and acquisitions as a key reaction this was intended to build cooperative energy, increment the scope of items and administration offering and sharing of thoughts.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter covers the research methodology that was used to achieve the study objective. It consist of the following sub-topics: research design, data collection and data analysis.

3.2 Research Design

The study used a case study research design. Neundorf (2002) explains that a case study design allows the researcher to carry out an in-depth investigation of the object under investigation. A case study was appropriate in enabling the researcher to identify the strategic responses used by Faulu bank to counter environmental challenges. This allowed the researcher to explore and to have an in-depth investigation of the unit of analysis concerning the study variables which are the strategic response to environmental challenges. This approach allowed the interviewer to interact with the interviewees on a one-on-one basis it gives the interviewees the freedom of thought to give their opinion without any bias and to provide detailed information about the study variables.

3.3 Data Collection

This study used qualitative data. This is because open-ended questions were used for data collection, these questions were non-numerical in nature and the information collected was based on the understanding of the interviewees on the concepts under investigation and their perceptions on the issues in question (Patton, 2002). Primary data was collected using an interview guide.

The interview guide consisted of three sections. Section A covered questions on general information about the interviewees and Faulu bank. Section B elicited questions on the environmental challenges affecting Faulu bank and Section C elicited questions on the strategic responses adopted by Faulu bank to cope with the environmental challenges.

A face-to-face interview was carried out by interviewing four departmental heads at Faulu bank. These departments were marketing department, finance department, operations department and research and development department. This category of interviewees was deemed to be highly involved either directly or indirectly on matters of strategy adoption and implementation and thus understood the strategic responses adopted by Faulu bank and the environmental challenges that it faces.

3.4 Data Analysis

Data analysis was done using content analysis which is a systematic and qualitative description of the composition of the objects of the study. Neundorf (2002) indicates that content analysis uses observations and detailed narrative of objects items or things that comprise of the unit of analysis.

Content analysis method focuses on distinct themes that illustrate a broad range of meanings of a phenomenon rather than the statistical significance of the occurrence of specific concepts. Maxwell (2005) indicates that content analysis is appropriate in providing details about the firm in particular on the study variables.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter consists of findings and discussion that have been done in line with the objectives of the study which were to determine the environmental challenges affecting Faulu bank and to identify the strategic response that it adopts to cope with these challenges.

4.2 Feedback Analysis

The researcher managed to interview all the four interviewees that were targeted. In all the interview sessions, the researcher had ample time with the interviewees that enable him to ask all the questions that he needed. The interviewees took their time patiently to respond to the questions asked by the researcher and thus adequate and more accurate information was gathered.

4.3 Background Information

Concerning the length of service of the interviewees, the findings revealed that three of the interviewees had served for more than three years while only one of the interviewees had served for more than one year. This was an indication that majority of the interviewees had a relevant experience in working for Faulu bank.

With regard to the position held by the respondents, the results found that the interviewees interviewed held the following positions: Head of Marketing, Head of Operations, Head of Finance and the Head of Research and Development. Further, the results found that the interviewees had served in their current positions for three years while only one of the interviewee had served in his current position for two years.

This was an indication that the interviewees were well versed with strategic responses that Faulu bank adopted to deal with environmental challenges.

Majority of the interviewees agreed that the fact that Faulu exposed them to various functions, they were not limited to their roles and this gave them exposure and increased understanding of Faulu bank operations. One of the interviewees indicated that the bank took so long to promote him and this made him feel as if his efforts were not recognized.

4.4 Environmental Challenges Facing Faulu Bank

The interviewees unanimously agreed that competition was a major environmental challenge that affected Faulu bank's operations. The banking sector in Kenya face rapid competition due to a number of factors that include technology, growth of the middle class, changing needs of the customer, liberalization of commercial banks and increase in the number of commercial bank players. This has however forced Faulu to find appropriate ways of coping with such kind of competition.

The interviewees indicated that innovative technologies changes had forced Faulu bank to adopt coping strategies to remain relevant in the banking industry. Faulu bank have adopted the use of Mobile Banking, Automated Teller Machines, Debit and Credit cards and Real Time Gross Settlement systems to enhance accessibility, convenience and flexibility of banking services to the customers.

One of the interviewees argued that some of these innovative technologies adopted by Faulu bank are more adaptable to environmental changes. The uniqueness of its products and services and lucrative interest rates have given Faulu bank unmatched innovation engine that locks out its rivals while guaranteeing Faulu bank high profitability of their businesses.

The interviewees also said that Faulu bank faced stiff competition by other market players who competed for the same buyers. This was a major challenge to Faulu bank because it posed a major threat to its survival especially on its growth.

The interviewees indicated that political instability was a major environmental challenge that affected the operations of Faulu bank. The interviewees cited instances of IEBC demonstrations that forced the bank to close some of its branches this exposed the bank to losses especially in cases when the bank had to close for long hours. These findings are consistent to Haunschild and Phillips (2014) who indicated that political risks prevent investors from making long-term financial commitment. Political instability is less attractive to both local and foreign direct investment. Firms are compelled to adopt short-term investments rather than long-term investments to minimize potential risks that might expose them to financial losses.

The interviewees agreed that complying with regulatory requirements and standards has forced firms to rethink about their strategies to deal with environmental challenges. The interviewees agreed that compliance with the set rules and regulations is a major challenge to most microfinance banks that are newly licensed since it hinders them from competing with commercial banks which are more stable with a huge asset base.

This is line with Castrogiovanni (2010) who argues that banking regulations ensure that firms do not engage in unfair business practices to avoid unfair competition. This provides a level playing field for the industry players to enforce compliance with market benchmarks.

The interviewees agreed that the customer needs are dynamic and they keep evolving. To cope up with the customer needs, Faulu bank adopts product differentiation to segment its customers and increase the scope of their market. This gives customers a wide array of products and services to choose from based on their specific needs and hence make products and services affordable to a wide scope of customers. These findings are consistent to Beckman; Haunschild and Phillips (2004) who observed that coping up with the changing needs and requirements is a major environmental challenge that firms have to cope with to remain relevant and competitive. Customers have different tastes and preferences and thus firms segment their customers to widen their scope of their target market and to serve diverse needs of the customers.

4.5 Strategic Responses Adopted by Faulu Bank

The interviewees stated that Faulu bank crafted a strategic plan which was part of its strategic response. The strategic plan was intended to cover a period of five years aiming to accommodate the environmental challenges such as competition in the banking industry and customers' needs. The interviewees indicated that the bank's marketing department was obligated to coordinate strategic responses in the organization. It was charged with the responsibility of gathering market intelligence and merging the views of the departments which was supervised by the managing director.

The interviewees indicated that previously, when the bank was a Deposit Taking Microfinance bank, it was limited in the products and services that it offered; the most popular one was the group based loans. The bank made tremendous efforts to align the bank structure and its products to its current status of Microfinance bank where it offers a wide variety of products and services such as both credit and savings products that suit the customers' diverse financial needs, Savings Products, Loan Products, Micro Insurance and Faulu Popote Service.

The interviewees pointed out that Faulu bank created a new department which was non-existent before; this department was legal department which was intended to counter the various challenges from legal and political challenges. This response strategy was intended to ensure that the banking operations and its products and services offerings are carried out within the regulatory framework and to prevent malpractices and unfair competition within the banking industry. This was intended to ensure that customers got access to quality banking products and services.

The interviewees unanimously agreed that Faulu bank had implemented product innovation as a strategic response to counter environmental challenges. The study found that Faulu bank had a business development department whose core activity was to develop concepts, ideas and innovative strategies to either improve the existing products and services or develop new products or services. The employees who work in this department were highly encouraged to come up with viable and unique ideas which could be converted into a product or service to improve the quality of the banking services and to make the bank more competitive in the banking industry. Further it was revealed that Faulu bank retained innovative and competent employees by giving them attractive salaries to continue to make their contributions in research and development.

The interviewees agreed that Faulu bank had a training and development programme which was conducted on a continuous basis. These programmes were part of the strategic responses meant to improve the level of employee skills and competences to boost their efficiency and professionalism in their work. This guaranteed Faulu bank quality services and professional services to their customers; this was part of the bank's strategic response that retained existing customers while attracting new ones.

All the interviewees agreed that Faulu bank adopted modern technologies for example Information Communication Technology as a strategy to address the changing needs of the customers and to improve the performance of the bank. The findings revealed that Faulu bank invested largely in modern technologies to enhance its level of efficiency in its business processes. It had a team of information technology experts that spearheaded most of the technological innovations implemented by Faulu bank. Notably, most of the banking products and services utilized modern technology for example the use of mobile banking, use of Automated Teller Machine, Use of Debit and Credit Cards. This response strategy was aimed at enhancing access to banking services, convenience, flexibility and cost reduction. Further, it was revealed that the bank engaged its employees in constant training and development programmes to improve their skills in the use of Information Communication Technology.

The interviewees indicated that Faulu bank adopted product differentiation as a strategy; this was intended to ensure that Faulu bank served a wide market segment to meet the diverse needs of all its customers. Faulu bank offered unique products and services that accommodated the lower-end customers who were previously ignored and forgotten by commercial banks. Through product differentiation, the bank made sure that its products and services were client-centered making them more attractive to the customers.

The interviewees agreed that Faulu bank's products were developed as a result of extensive market research to ensure they delivered value adding products and services to satisfy their customers. Each of Faulu bank's products or services was carefully designed to address the customers' financial needs. As part of the bank's vision, the interviewees indicated that Faulu bank was committed to serve its clients with relevant products and transform their lives and those of their families.

The interviewees stated that Faulu bank allocated a huge budget for research and developing to effectively understand the market trends, customer needs and the external environment. This provided a platform for innovation, product or service development since Faulu bank was able to offer product and services whose attributes were aimed at serving specific financial needs in the market that were underserved or not taken care of completely.

The research and development team collected the views of customers based on their different experiences on the products and service offerings. This was intended to establish whether the customers were satisfied with the form of product differentiation strategy that was utilized by Faulu bank and the areas that needed improvement.

The interviewees, further indicated that Faulu bank needed to invest more in research and development and modern technology in order to offer more integrated services that are efficient and less costly that add value to the customers. They argued that through this approach Faulu bank could attract more customers and boost its sales growth.

In addition with, the interviewees agreed that Faulu bank had a training and development programme that enabled the employees to learn specific knowledge and skills in their apparent roles. Faulu bank considered development more expansive and it focused on growth of the employees and their future performance rather than an immediate job role. training and development programmes was part of Faulu bank strategy commonly used by firms to improve its employees' skills and knowledge to boost efficiency and professionalism in their work.

Further, the findings revealed that the main objective of these training programmes was assisting the employees to learn specialized knowledge and skills and to improve performance in their current roles. Training and development programmes aided Faulu bank to retain the right employees and growth profit. To effectively deal with changing needs of the customers, training and development was presumed to provide a wide range of learning actions, ranging from training of the employees for their present tasks and more so, knowledge sharing to improve the business horizon and customer's service.

A comprehensive training and development program was intended to enhancing the knowledge, skills and attitudes necessary to achieve organizational goals and also to create competitive advantage over Faulu bank's rivals.

The interviewees agreed that talent management was part of Faulu bank's strategic response which was aimed at attracting and retaining competent personnel that could contribute effectively in making invaluable contributions.

Faulu bank's talent management programmes involved identification, development, engagement; retention and deployment of employees who could add value to the bank whilst promising a high potential for Faulu bank's future and achieving its operational roles. Faulu bank recruited and selected talented employees who had a potential to perform highly.

Faulu bank's strategic talent management approach to attract, develop and retain employees who were capable to meet the current and future needs of the bank. Faulu bank adopted a strategic talent management model to create a path and design a reward plan to the top performing employees. This was intended to ensure that the bank hired the best professionals who were competent and efficient.

The interviewees indicated that the main objective of having a strategic talent management programme was mainly to ensure that Faulu bank had the right employees with the right skills and knowledge. This was achieved through a complete set of process for recognizing, managing employees to ensure successful business strategy that was integrated with Faulu bank's vision and mission.

The interviewees agreed that Faulu bank management executive focused on retaining talented employees in order to exploit their skills, ideas and efficiency in enhancing Faulu bank's competitiveness. Further, the findings revealed that the top management communicated clearly to the employees concerning the strategic business objectives across the bank and provided clear directions on how set goals were to be realized.

The interviewees agreed that as part of their strategic response, Faulu bank conceded an acquisition of 67 per cent controlling stake by Old Mutual. The deal involved immediate injection of Sh2.8 billion of the Sh3.6 billion agreed price, after successful fulfillment of all required regulatory approvals and closure of the transaction.

The interviewees indicated that Faulu bank accepted the acquisition to benefit from synergy, a wide variety of products and services, reduced risks, capital base and ideas. In so doing, the bank has been performing better in terms of growth of its customer base and improved profitability.

4.6 Discussion of Findings

Competition was a major environmental challenge that affected Faulu bank's operations. This competition is as a result of technological changes, growth of the middle class, changing customer needs and liberalization of commercial banks. These findings are consistent to Beckman, Haunschild and Phillips (2004) who argue that competition is one of the main challenges facing the banking industry in Kenya.

The other challenge that faced Faulu banks in Kenya was lack of adequate finances to investment in research and development for innovation purposes. These findings are consistent to Beckman et al. (2004) who contended that most firms in the developing countries lacked funds for to carry out research and development this impacted negatively on the innovation.

Political instability was a major environmental challenge that impacted negatively on Faulu bank's operations. The interviewees cited instances of IEBC demonstrations that forced the bank to close some of its branches this exposed the bank to losses especially in cases when the bank closed for long hours. These findings are consistent to Haunschild and Phillips (2014) who indicated that political risks prevent investors from making long-term financial commitment. Political instability is less attractive to both local and foreign direct investment. Firms are compelled to adopt short-term investments rather than long-term investments to minimize potential risks that might expose them to financial losses.

Complying with regulatory requirements and standards was a major challenge that forced Faulu bank to rethink about its strategies to deal with this issue. The findings indicated that the regulations made it difficult for newly licensed Microfinance banks to compete with other commercial banks that were stable in terms of asset base. These findings are consistent to Dondo (2001) who argued that it was difficult for newly licensed Microfinance banks to compete with commercial banks because of compliance with regulatory requirements.

Coping with customer needs and requirements was a major environmental challenge that faced Faulu bank. The needs of the customers keep on changing and coping with such needs is not easy. These findings are consistent to Castrogiovanni (2002) who indicated that meeting customer needs is one of the most difficult tasks faced by most firms this is because customer needs keeps on evolving.

To cope with environmental challenges Faulu bank adopts strategic responses as follows: Faulu bank crafted a strategic plan which was part of its strategic response; this plan was intended to address the challenges that Faulu bank faced such as competition. These findings are consistent to Thompson (2008) who emphasized on the need to have a strategic plan to effectively respond to environmental challenges.

Faulu bank had a wide variety of differentiated products and services to meet the needs of all its target customers. These findings are consistent to Johnson and Scholes (2002) argue that the through differentiation of products and services the firm is able to target a wider market segment that allows all classes of customers to have access to products or services which they can afford.

Faulu bank adopted product innovation to counter environmental challenges. The bank had a business development department whose core activity was to develop concepts, ideas and innovative strategies to either improve existing products and services or develop new products and service. This was meant to continuously address customer needs. This is consistent to Geroski (2008) who maintained that product innovation enabled companies to provide cheaper and high-quality services to enhance customer satisfaction.

Faulu bank had a training and development programme which was conducted on a continuous basis. This enabled the bank employees to offer quality and professional services to their customers. In view of this, Brass et al. (2004) indicated that training and development programme enables employees to sharpen their skills and increase their knowledge in their work which impacts positively on the quality of services offered by the firm.

Faulu bank utilized modern technology such as ICT to enhance efficiency in banking operations. This sought to achieve increased access to banking services, convenience, flexibility and cost reduction. These findings conform to Geroski (2008) who insisted on the need for a firm to invest in modern technology to achieve integration of business processes and procedures to enhance efficiency and minimize cost. In so doing, this enables the firm to gain a competitive edge over its competitors.

Faulu bank adopted a strategic talent management approach to attract, develop and retain employees who were capable to meet the current and future needs of the bank. This was achieved by formulating strategies and making key decisions on ways to cope with diverse needs of the customers to remain competitive in the banking industry. The bank hired the best professionals who were competent and efficient. These conforms to the observations made by Johnson and Scholes (2002) who indicated that a strategic talent management programme is one of the best approach used by firms to ensure that they have a competent team of employees that can make accurate decisions to ensure that the firm remains competitive in the market. Talented employees are passionate about their work hence offer the best quality services to their customers.

The interviewees indicated that Faulu bank accepted the acquisition to benefit from synergy, a wide variety of products and services, reduced risks and capital base and ideas. These findings are consistent to Thompson (2008) who argued that firms adopt mergers and acquisitions to benefit from reduced costs of operations, expansion of geographic coverage, expansion of the organisations business and products portfolio and access to modern technologies.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter consists of the summary of the findings, conclusions drawn from the findings and the suggested recommendations for the study. The conclusions and the recommendations were made in an effort to address the study objectives which were to determine the environmental challenges affecting Faulu bank and to identify the strategic responses adopted by Faulu bank to cope with the environmental challenges.

5.2 Summary of Findings

The study found that the major challenge facing Faulu bank were the following, the dynamic nature of technology and banking innovation which was a major challenge that forced Faulu bank to adopt coping strategies to remain relevant in the banking industry. Secondly, political instability affected the normal operations of the bank. They cited instances where demonstrations by IEBC forced led to the closure of their bank branches where these demonstrations took place. Based on the findings such events contributed to huge losses for the banks. Thirdly, complying with the regulatory requirements impacted negatively on bank's performance especially due to competition from commercial banks. This attracted high costs which impacted negatively on the performance of the bank. Fourthly, the fact that the changing needs of the customers keeps on changing is a major challenge to Faulu Bank. This forced the bank to set aside a huge budget for research and development to understand the needs of the customers and to tailor their products and services to those needs.

The study found that Faulu bank adopted strategic responses to cope with environmental changes. Faulu bank had set up a legal department that ensured that their products or services offering complied with the regulatory framework. They indicated that Faulu bank implemented product innovation as a strategic response to counter challenges in the environment. Faulu allocated a huge budget for research and development that was charged with the responsibility of products development to ensure that the products or services offered by Faulu bank were tailored to suit customer needs. Secondly, Faulu bank adopted ICT to enhance integration of products and services. Based on findings, the interviewees indicated that the use of ICT was meant to improved efficiency in banking operations. The bank used product differentiation to expand its market segments to meet the different needs of the customers. Product differentiation aimed at targeting the lower-end by increasing their accessibility of banking products and services. Further, the bank had a continuous training and development programme that was conducted on a continuous basis to improve skills and competence of employees. Also, the bank had a strategic talent management programme that attracted and retained talented and gifted employees to contribute their energies towards achieving the bank's goals. The decision by Faulu bank to concede an acquisition by Old Mutual was part of its strategic response which was aimed at strengthening Faulu bank's asset base, widening the scope of their products line and innovation.

5.3 Conclusion

The study concluded that the environmental challenges that faced Faulu bank were competition, obsolete technology, evolving customer needs, complying with regulatory requirements and political instability. It was observed that these challenges hindered Faulu bank's survival in environment and thus necessitated the adoption of strategic responses to remedy the situation.

It was further concluded that the main strategic responses adopted by Faulu bank to deal with environmental challenges included the adoption of product and service innovation, use of modern technologies, product differentiation, investing in research and development programmes, strategic talent management programme and training and development programme. These strategic responses were meant to enable Faulu bank to counter environment environmental challenges and to remain competitive in the market place.

5.4 Recommendations

The study recommends that Faulu bank should increase its budgetary allocation on research and development to enhance innovation in the existing products to allow firms to develop new products and adopt better approaches to produce quality products and services.

Faulu Bank should invest more on information communication technology to achieve system integration; this will increase sharing of information and communication in the bank hence boost efficiency in banking operations and decision making. This will minimize both communication and supervision costs by Faulu bank.

Faulu bank should formalize employees' training and development programmes to improve their skills and knowledge on their work. This will motivate the employees to perform their duties and contribute positively towards achieving their set targets.

The study further recommends that Faulu banks should integrate strategic talent management programs in their strategic plans. This will ensure that Faulu bank has skilled and competent employees who can share in the same vision and thus work towards realizing similar goals and objectives.

5.5 Limitations for the Study

Due to time and cost constraints the study limited itself to Faulu bank. The results obtained in this study cannot be used for direct application in any other Microfinance bank or the entire banking industry in Kenya; this is because these results are unique because the way Faulu responds to environmental challenges might be different from other Microfinance banks. The findings would have been more accurate and reliable if the researcher had time to study all the Microfinance banks in Kenya.

5.6 Suggestions for Further Research

The study further recommends that a study should be carried out to establish the influence of strategic responses on organizational performance laying more focus on the reduction of costs and improved efficiency.

Finally, future researchers should investigate the impact of strategic responses on long-term sustainability of microfinance banks in Kenya. The study should concentrate on specific variables that contribute to sustainability of strategic responses for example product innovation to continuously address the changing needs of the customers.

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APPENDICES

Appendix I: Introduction Letter

Dear Sir/Madam

RE: DATA COLLECTION

I am a post graduate student at the University of Nairobi, undertaking a Master of Business Administration. As part of my course I was required to carry out a research on the strategic responses to environmental challenges facing Faulu bank in Kenya. Faulu bank was selected to be part of this study and was kindly requested to assist the researcher to collect data by accepting to participate in the interview process and to respond to all the questions asked. This information treated with a lot of confidentiality and it was solely for academic purposes.

Your assistance will be highly appreciated.

Yours faithfully

Appendix II: Interview Guide

This is an interview guide for collecting data on the strategic responses to environmental challenges facing Faulu Bank in Kenya.

A: Interviewee's Background

1. How long have you served in this bank?
2. Which position do you occupy in this bank?
3. Have long have you served in your current position?
4. What do/did you like best about the positions/ you have held?

B: What are some of the environmental challenges facing Faulu Bank?

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C. What strategic responses does Faulu bank adopt to address each of the challenges Mentioned Above?

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