

**ISLAMIC BANKING STRATEGY AND STRUTURE OF ISLAMIC COMMERCIAL
BANKS IN KENYA**

BY

SALIMA WARUIRU KIBATHI

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DECLARATION

This research project is my original work and has not been submitted for examination in any other university.

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Salima Waruiru Kibathi

D61/81071/2015

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DATE

This research project has been submitted for examination with my approval as the University Supervisor.

.....

Dr. Mary Kinoti

Senior Lecture, Dept of Business Administration

School of Business

University of Nairobi.

.....

DATE

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DEDICATION

To my parents H. Kibathi and the late mother Mwanaisha Kibathi who will always be the noor of my eyes.

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ABBREVIATIONS AND ACRONYMS

ANOVA: Analysis of Variance

CBK: Central Bank of Kenya

GAB: Gulf African Bank

KCB: Kenya Commercial Bank

RBV: resource Based View

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ABSTRACT

The banking industry in the last few years has experienced changes both in the strategy formulation and structure framework. These coupled with the highly competitive environment has forced most banks to formulate strategies that will ensure they gain competitive advantage over their rivals and align both strategy and structure. The research was carried out with the aim of analyzing Islamic banking strategy and structure of Islamic commercial banks in Kenya. Descriptive research design was adopted in this study. 8 banks took part in this study in which 6 banks duly responded. Primary data was used in this study. Questionnaires were used to collect the data. The respondents held the position of managers and shariah board in their respective organizations. Descriptive statistics and especially SSPS were used to analyze the data. The effect of Islamic banking strategy and structure of Islamic commercial banks was investigated using chic square analysis method. From this study the researcher found out Islamic banking strategy is associated with various performance indicators which are both financial and non-financial and that customer loyalty, cost leadership, price leadership, product differentiation and reputation influence Islamic banking strategy. This study recommended that Islamic banks as well as the commercial banks offering Islamic products and services should review their strategies regularly within less than five years so that they are able to meet market and organization demand in offering of Islamic products and services and they should develop clear guidelines on their shariah compliance regulations. Further studies should focus on pure Islamic banks for generalization of the findings.

CHAPTER ONE

INTRODUCTION

1.2 Background of the Study

Strategic management is a field that deals with the emergent and intended work of an organization. It involves use of resources and managers involvement to build on the performance of the organization. Strategic management provides overall direction of the organization through specifying its vision, mission, objectives, developing policies and finally allocating the resources needed in implementing the policies in place (Pearce and Robinson, 2002). An organizational strategy governs the whole organization and sets the direction in which they will move to. Strategy gives the direction in which a firm should move into. It is through the development of a strategy that managers are able to identify critical matters that need to be addressed in current activities as well as long term objectivities. According to (Porter, 1985), is that the goal of a strategy is to ensure enduring competitive advantage over its rival.

For a strategy to be implemented successfully the structure has to be place. The already existing structure also determines how an organization will pursue specific strategy and the capacity it holds. Any changes that takes place in the environment led to organization reorganizing their strategy and therefore changing their structure so as to adapt to the environment. Organizational structure defines how activities will be achieved through providing a foundation on which standard procedures will be based and decide who will participate in decision making process (Wheelen and Hunger 2008).

Several theories explain the concept of strategy and structure. They include system theory developed in 1954 by Ludwig Von Bertalanff, contingency theory developed in 1964 by Robert Blake and Jane Mouton and resourced based theory developed in the early1950and published in 1959 by Penrose. According to the system theory, organizations are systems that are able to interact with the environment and can adaptively respond to environmental changes (Friedman & Allen, 2004). On the other hand contingency theory suggest that there is no best way of doing things and that one successful leadership style might not always work for some situations

(Donaldson, 2001). As for resource based theory, it is based on the assumption that for a firm to gain competitive advantage it has to have resources, capabilities and competencies (Grant, 2010). These theories will provide important guidelines for the study.

The banking industry is faced with environmental changes among them being interest rate capping, high cost of borrowing, theft cases, regulatory pressure and global financial crisis. Interest rate capping placed by the government has dented the bank's ability to make profit and to provide returns to the shareholders. On the other hand high cost of borrowing and global financial crisis is making it hard for customers to borrow from banks and this is a problem since borrowing is a major income to all financial institutions. Banks are also facing theft cases from employees, security providers and other external individuals which in the end taint the image of the institution in place. (Banking survey, 2009).

1.1.1 Concept of Strategy

Strategy has been defined variously by different authors. Quinn (2003) describes "strategy as a pattern or plan that integrates an organization's major goals, policies and actions sequences into a cohesive whole". A strategy that is well formulated help distributes organization's resources evenly depending on internal competencies, changes that take place in the environment and actions of the competitors. This is in line with the work of Yabs (2010) and Johnson et al (2008) who further described strategy as "a pattern of major objectives, purpose or goals and essential policies or plans for achieving those goals".

Daft, (2010) concluded that "a strategy is a plan for interaction with the environment for purpose of competition to attain goals set by organization and the choice of a strategy affects internal organization characteristics". Based on the above definitions there is consensus in choosing a unique strategy and set of activities that are difficult to imitate and are different from the competitors in order to deliver the right values to the customers. Strategy is a critical factor for gaining competitive advantage and great performance (Capon, 2008). The banking strategy should enable the organization gain competitive advantage through delivering benefits similar to competitors but at a cost that is lower or through exceeding customer's expectations (Porter 1980).

Strategy is broken into three different levels. They include corporate strategy, business strategy and functional strategy. Corporate strategy describes the type of business an organization should be in and how value can be added in different departments of the organization. This includes geographical areas, diversification of products and resource allocation. Business strategy is concerned with how an organization gains competitive advantage through successfully competing in the external environment. It involves the product to be developed and in which market they should compete in. The third strategy is the functional strategy which is concerned with how different sub-sections of organization work together to deliver overall strategy through proper use of people, resources and processes (Carpenter and Sanders, 2009).

Organizational strategy plays an important role which includes: provide direction, align activities, defines accountabilities, enhance communication, provide a framework for decision making and resource allocation. It provides the direction in which the organization wishes to be in and the action plan that will assist them in achieving those goals. It also aligns all the activities that are necessary in achieving the desired results. This is through drawing clear lines of accountability for achieving desired results and this can be achieved through proper commitment and communication at all levels (Johnson and Scholes, 2002). Strategic implementation then follows and it is the sum total of activities required so that a strategy can be executed (Hunger and Wheelen, 2003).

1.1.2 Organizational Structure

The term organizational structure has been defined variously by different authors. Pearce and Robinson (2002) described structure as “a system of tasks, workflows, reporting relationships and communication channels that link together the work of diverse individuals and groups. It is providing for decentralizing and centralizing that is consistent with the organization and control needs of the strategy”. Jones, (2010) further described organizational structure “as a system that is formal in nature and control how people coordinate their actions through authority and use resources to attain organizational goals”.

Organizational structure ensures it achieves overall goals through ensuring the actions of the people are in line and to ensure the method used to motivate people are to the standard of the establishment. “Organizational structure is a system of arrangement that support patterns of relationships within an enterprise and support various positions which are characterized by authority relationship” (Bhattacharyya and Kumar, 2009).Thompson, (2000) concluded that structure “is organizational pattern of relations, author and communication”.

Organization structure has significant importance in communication, support of functional areas, achieving goals, employees’ evaluation and provision of solutions. Organization structure facilitates proper communication through line of authority. It also supports different functional areas within the organization through ensuring the all persons understand their responsibilities. A strategy does not function well unless the existing structure parts are reinforcing each other and are supporting the overall strategy (Thompson and Strickland, 2002).This closely follows with evaluation of employees’ skills by their supervisors and providing solutions by managing changes that take place in the external environment (Jonson et al, 2008).

Organizational structure is governed by three dimensions: centralization, formalization and complexity. Centralization is the degree in which to make decision is given to those in authority, while formalization is where rules and regulations are used to describe behavior through matching formalization and professionalism. Lastly complexity is about combining different aspects of the organization (Pearce and Robinson, 2011). There are three main types of organizational structure that govern this dimensions and they are: functional, divisional and matrix structure. Functional structure is grouping of organization according to its purpose. Secondly divisional structure is grouping according to the product or market available and lastly matrix structure is a hybrid of functional and divisional structure (Daft, 2010).

1.1.3 Commercial Bank of Kenya

In 1966 the central bank of Kenya was established under the parliament Act and became public in September the same year. The purpose of the central bank of Kenya was to formulate and implement monetary policy that promotes price stability. The central bank of Kenya governs the banking industry in Kenya. It has the responsible for ensuring the monetary policies are properly

formulated and functioning within the financial system. There are forty three financial institutions in Kenya, thirty five of which are locally owned while the rest are foreign owned. The industry is dominated by large banks which are foreign owned with a few partially locally owned. Over a number of years the banking industry in Kenya has grown in terms of deposit, assets, product offered and profitability. This has been demonstrated through wide branch network expansion strategy such as customer service, innovative products and creating new organizational structure (Kenya bankers' association annual report, 2008).

1.1.4 Islamic Commercial Banks in Kenya

In Kenya, Barclays bank became the first bank in December 21st 2005 to launch Islamic banking products when it launched La Riba account an interest free bank account. On May 29th 2007 First community bank was the pioneering bank in Kenya authorized by the CBK to operate as a full-fledged Shariah Compliant banking institution and it commenced operations on 1st June 2008 (First Community Bank, 2016). In the same year GAB opened its doors and become the second fully shariah compliant bank in Kenya.

Several conventional banks then followed in offering Islamic banking services. These include Barclays bank, National Bank, Standard Chartered and KCB. Islamic banking accounts to 2% of the share market in Kenya where Muslims make up 15% of the population of 40 million. As such the 2 fully fledged Islamic banks are in tier 3 of banks in Kenya. There is therefore need to explore strategies by these banks to attract customers and increase their market share in the highly competitive banking industry (Vizcaino, 2016).

Implementation of Islamic shariah laws in the banking system in Kenya is an important guideline in all commercial banks as the quest for Islamic banking practices continues to persist hence each commercial bank has to lay down its competitive strategies and align themselves with the ever growing market niche and changing environmental trends. Most commercial banks are striving to come up with the best strategic plan that will give them a competitive edge and guide them in their operation on how to handle the growing market niche that focus on Islamic banking system. This is evidenced by the fact that there are eight financial institutions that are competing

to offer Islamic banking system in Kenya (Vizcaino, 2016). By 2010, their banking assets had increased to 0.8% and 1% respectively (Chijoriga and Kaijage, 2012).

Islamic banks have shown significant growth in the area of capital amount, gross assets, deposits and profit after tax and this is due to different strategies that they have put in place to support the growth of the financial sector in Kenya. They offer different services and facilities such as the personal saving, business facilities, foreign currency to term deposit, financing trade facilities, construction, SMES' mortgage facilities and asset based financing (Mustafa, 2012).

1.2 Research Problem

Organizational strategy aims at making profit and correctly positioning itself against industry and environmental forces (Porter, 1985). It is part of organizational strategy to compete and achieve management plan. According to Porter (1980), the importance of formulating a strategy is to ensure a company matches with the environment. Environment is the means by which organization survive and it is also the source of the most immediate layer surrounding the organization (Johnson & Scholes, 2008)

Organizational structures must align itself with the strategy to facilitate achievement of organizations' purpose, the needs for organizational change in the business environment and allow the smooth functioning of organization technologies. If not well selected, poor organizational structure can lead to low employee morale. In addition, poor organizational structure can lead to overall delays in decision making process, lack of co-ordination, failure to innovate, and escalating administrative costs which will make the organization largely inefficient, very expensive to run and ultimately uncompetitive in the contemporary highly dynamic market environment. Organizational structure is a means by which communication is established throughout the organization from top management to lower level management. A poorly designed structure led to lack of proper monitoring system (Fuchs and Becks, 2004).

Islamic banking only makes up 2% of the total banking business in Kenya while the Muslim population is roughly 15% of the total 40 million (Vizcaino, 2016). Several studies such as Erol & El-Bdour (1989), Ahmad & Planisek (1994) have concluded that religion is not the main

factor attracting customers to bank with Islamic windows or fully shariah compliant banks, other factors such as efficient services, reputation and confidentiality influence a person's decision.

Islamic banks have had to look beyond religion to attract customers. As such Islamic banking should understand that religion factor and number of Muslim clients should not be the only strategy used to attract consumers. This realization has forced Islamic banks to come up with strategies that will aim to give them competitive edge over their rivals and also attract customers across all religions.

Although many studies have been done in the area of strategy and structure, their findings and recommendations are not applicable in Islamic banking system because the context and time are different. In the international context Miller, (2002) did a research on configuration between strategy and structure and found a strong configuration and relationship between strategy and structure. Al-ajlouni (2007) did a research on strategies used by Islamic banks to overcome future financial and globalization challenges in Malaysia and concluded that Islamic banks have to adapt to operational and globalization strategies for them to attain a competitive edge. Haron and Azmi (2005), did a research on Islamic banks marketing strategies and concluded that the strategies that attract and retain customers should be used to give them an edge over the rivals.

In the Kenyan context, Issak & Kaswira (2012) studied the strategies that are used to achieve growth among banks that offer shariah compliant products and concluded that these financial institutions need to ensure there is strict following of shariah in their day to day operations. Mutua, (2012) dealt with strategy and structure alignment at Barclays bank and found out that that there is a great relation between strategy and structure and those organizations that can obtain a fit between strategy and structure will increase their competitive edge. The study concluded that sometime change in strategy have minimal impact on structure. Kavale, (2012) carried out a study on the connection of strategy and structure and concluded that it is the responsibility of the top management to continuously monitor the organizational structure and align them to the remote environment. Finally, Essajee, (2011) looked at the difficulty of implementing strategy and concluded lack of knowledge, customer perception and few differentiation of products was the reason to it. There is a knowledge gap that exists because none of them dealt on Islamic banking strategy and structure of Islamic commercial bank.

Strategies give competitive edge to firms over their rivals and studies such as Bowen & Ostroff (2004), have shown that competitive strategies leads to improved performance. Islamic banking is a fairly new phenomenon in Kenya. Islamic banks cannot only relay on religious factor as to be attractive enough to pursue customers of the Islamic faith to use the facilities of these shariah compliant banks (AbuBakar 2003).

It is very easy for customers to switch from one bank to another, operate various accounts in different banks and access facilities from more than one bank at the same which will impact the performance of these banks. Therefore Islamic banks need to apply competitive strategy so that they can establish profitable and sustainable position in the highly competitive industry. The research will adopt the following research question: what is the effect of Islamic banking strategy on structure of Islamic Commercial banks in Kenya?

1.3 Research Objective

The main objective was to determine how Islamic banking strategy influences organizational structure of commercial bank in Kenya.

1.4 Value of the Study

The study will provide a reference point for all academicians who want to engage in research and it will provide more information to the existing body of knowledge by providing empirical evidence that can be used in research by scholars and researchers. Further study can also be carried out by Islamic banks in Kenya who feel the need of improving the state shariah law implementation.

The research will influence practitioners in the way they make decisions and coming up with the best strategies that will support organizational structure. The Islamic/ shariah compliant is fairly a young industry and the study will act as a basis for further research in the area of strategy and structure used by Islamic banks and bank regulators. The management will gain more knowledge on how to ensure that their strategies fit with the structure in place.

The research will guide the government in designing proper policies and regulations that guide Islamic banks in Kenya and promote the integrity of the banking systems in Kenya. Policymakers will also get an insight on how to best come up with policies that will guide Islamic banking systems and ensure that there is high level of efficiency.

This study will help in facilitating theory testing. It contributed to the current knowledge on system theory, contingency theory and resource based theory. It will help in investigating the main concept of resource based theory that links the growth of an organization to how the resources of the organization are utilized. The study will also help in testing the concept of contingency theory that an organization needs to exploit its current internal and external organization which will fit with the main structure.

CHAPTER TWO

LITERATURE REVIEW

This chapter carried out an in-depth analysis of existing literature that has been done by other scholars. It relate to theoretical underpinning, Islamic banking strategy and its impact on structure of Islamic commercial banks. This section offered an in-depth understanding of the relationship between strategy and structure and also established the research gap that this study filled.

A literature review is a pattern of the organization and a summary combination that synthesis knowledge. It looks at all important information of the sources through ensuring information is well organized. All the old material is interpreted again. It gives progression to the field of study and evaluates the sources and this is through synthesis of the arguments made by others without adding new contributions (Podsakoff et al, 2003).

Literature review relates each work to the contribution made to the research problem being studied and describes the relationship that exists between each one of them. It identifies different ways to make sense of previous research through revealing gaps that exist in the literature review. By understanding the gaps in place, it is able to prevent repeating information and solve conflicts caused previous studies that are different from others. It points the way in fulfilling a need for additional research and how to relate within the context of existing literature (Podsakoff et al, 2003).

2.2 Theoretical Foundation

This study was based on three theoretical foundations namely: system theory, contingency theory and resource based theory.

For companies that need to develop strategies the resource based theory and the system theory are said to be the two popular and competent ways of developing organizational strategy Williamson, (1991). The resources and system of an organization influences on a large extent the long term strategy of the organization because of two reasons; firstly, the profit of the company

is derived from the resources and system of the organization and secondly, the direction the firm intends to undertake or is already undertaking will be heavily influenced by the resources, capabilities and systems in place (Grant 2001).

Contingency theory will help managers respond to cases of individual problems rather than the problem itself by seeking to understand the influences that lead to difficulty that take place within the organization. The theory will also encourage managers to think about the decisions they make because of the consequences it might bring to whole company and be able to integrate variety of inputs (Grant, 2001).

2.2.1 System Theory

The system theory dates back in the early 1950 with the work of Ludwig Von Bertalanffy who stated that an organization is considered to be a functional system that is composed of interrelated parts that are able to interact with each other. All segments of an organization are intertwined to each other and action of one segment of an organization affects the rest in a varying degree. The system theory argues that managers of any organization can no longer confine themselves in the traditional organizational chart and they must ensure that all departments work together. It is only through having commitment of matching all employees and departments together that success is achieved. A system is considered to be either open or closed. An open system has the ability to interact freely with the environment. It is organizational internal or external ability to adapt to the changes its environment. When an organization has the ability to processing environmental information quicker it is considered to have higher adaptation skills. A closed system does not have interaction with its environment and if it does it is to a certain degree (Wang, 2004).

According to Ludwig Von Bertalanffy, system theory has enabled people to understand different components of a system that make up a whole that has enabled problem interpretation and development of invention strategies with the goal of uniting people to their environment. System theory does not have a specific theoretical framework that is able to interpret problems (Barney, 1991).

The theory further states that there are two conditions that govern the system theory and both of them have to be present for the system to be measurable. They include interaction between different parts and the condition describing the different parts. It is through an understanding of the system that managers within bank systems are able to look at organization from a bigger perspective which help them interpret patterns and events (Friedman and Allen 2004).

2.2.2 Contingency Theory

The contingency theory approach view was developed in 1964 by Robert Blake and Jane Mouton and states that the approach used by management and proved to be successful might not work in all situations. It suggests that some methods that were used in an organization and were highly successful in one situation and failed to work in others (Stoner et al, 2004).

The theory suggests that, it is management's duty to seek the best techniques that will be able to contribute to the goals of the organization at that particular time. The contingency theory serves an important role of ensuring that each organizational relationship and roll is treated uniquely. Organizations always choose contingency that fit with overall structure and always work with alignment with each other (Stoner et al,2004).

The theory suggests that the success of any organization comes from fitting the characteristics of the organization such as the main structure to the contingencies such as environment, organizational size and the strategy. Contingency theory is affected by the rate of environmental changes and the type of technology that will determine if its structure will be organic or mechanistic. Mechanistic structure is more stable as it allows managers at the upper level to make more solid decisions based on knowledge and information that they already acquired. In contrast organic structure is used for a less stable environment such as the lower level hierarchy (Donaldson, 2001).

The theory explains that any organizational structure needs to fit with the external environment, size of the organization and the overall strategy. Each of them affects a particular area of a structure such as organic, bureaucratic and division. Any changes that take place in one of them

affect the overall structure and thus there is need to align these contingencies with the structure so that structure and contingency are associated with each other (Donaldson, 2001).

2.2.3 Resource Based Theory

RBV theory developed in the early 1950 and among the early studies was by Penrose 1959, who proposed that the internal capabilities of any organization will led to competitive advantages over other key players in the market. The theory is governed by two assumptions; the first assumption is that skills that people poses, what they are capable of and other resources differ from one organization to another. If all organizations shared the same resources, there would not be any new strategies to outdo the other. The second assumption is that the resources available are mobile and do not move from one organization to another. For this reasons companies cannot use the same resources and strategies to outdo the other (Grant, 2010).

The success and growth of any organization is determined by how well resources are distributed both internally and externally. Every organization has a certain amount of resources within it and for an organization to grow and prosper it requires all its resources to be distributed evenly. An organization must be able to understand its strength and weakness in terms of resources and be able to outshine its rivals using its available resources. The resources are either tangible or intangible and they include organizational assets, human assets, financial assets, physical assets and technological assets which support innovation and growth of organization (Wernerfelt, 1984). Organizational success is governed by the assets of the firm and resources which reflect on how well they compete in the market place. The features of any of organizational resources should be hard to imitate and unique in nature. Through resources based theory firms can determines the amount of internal resources that a firm has that will enable it to compete and establishing the best strategy (Sheehan & Foss, 2007).

Resource based theory holds that organizations valuable resources are the ones that determine the performance and competitiveness of the firm. Resource based theory states that the major forces that influence and impact on the competitive advantage and how excellent an organization performs is derived from the features of the company's resources and capabilities which are both valued and hard to imitate (Barney, 1991). Through resource based theory firms can design and

carry out their firm strategy by looking at the position of their internal resources and capabilities Sheehan & Foss (2007).

2.3 Organizational Strategy

Organizations require a sustainable and working strategy to compete successfully in the industry against both current and potential rivals (Achoki, 2013). The choice of a strategy to will be used to gain competitive edge over rivals is an exact process (Capon, 2008). Capon (2008) also argues that for superior performance to be achieved strategy is a critical factor in any firm.

According (Porter, 1985) competitive advantage is gained through three generic strategies. They are cost leadership strategy, differentiation strategy, focus strategy. When a firm becomes the cost leader in the industry by producing at low costs and applying economics of scale it is said to have adopted cost leadership strategy. Cost leadership can be successful if a firm enjoys a huge market share relative to its rivals (Hyatt, 2001). Differentiation strategy is offering products and services that have unique features. According to Svatopluk and Ljuba (2006) differentiation strategy objective is to establish the main differences between the products the firm offers and those of its rivals. These unique differences are the ones that ensure these firms can demand for a premium price. This results in better returns and ultimately better performance than the firm's rivals.

Porter (1994) states that focus strategy involve identifying a niche market segment and developing products to satisfy the niche customers. This could lead to an increased customer and brand loyalty to the products and services of the firm. The business can position itself to increase brand loyalty and customer satisfaction through focusing the marketing mix on the narrowly defined market (Maina, 2014).

By concentrating the small but demanding segment that are willing to pay for premium prices a firm can achieve superior profits and overall performance (Anderson, 2006). Focus strategy is based on serving a narrow scope that most competitors do not get involved with (Maina, 2014).

2.4 Organizational Structure

Structure is a means by itself that is used to hold the whole organization together so as to determine the direction in which they are moving into and its future (Burns and Stalker, 1961). Organizational structure can be classified according to different models depending on its nature and they include mechanistic and organic structure. Mechanistic structures are those that have hierarchy of responsibilities and have a narrow scope, while organic structures are those that have few rules, ambiguous responsibilities and wide scope. Organic structure is best used when dealing with unstable and turbulent environment that has high degree of information sharing and low degree of formality (Pearce and Robinson, 2011).

There are different functions as to why organization structure exist and they are as follows: a formal allocation of work rules, a channels for working together, line of communication and levels of authority, allocating of responsibilities and where different levels of formality are described (Eccles et al, 1997). A structure operates best in a small organization than a large one and this is because the distribution of authority, task and responsibility are on a more personal and informal basis within a small organization. However as the sizes increase there is need for greater attention and continuous review on the structure to ensure that growth and development is been established (Mullin, 2010).

2.5 Strategy and Structure

The strategy must align itself to existing environment. Environment forces have a significant influence on both strategy and structure in place. Therefore firms must align with the turbulence and dynamism within the environment. Environmental forces influence the organizations through the changes it places on them. Strategists identify a structure to match with the strategy once strategy has been directed by the environmental forces, (Johnson et al, 2008).

Strategic alignment follows and it is through aligning the strategy and the structure to the environment. The strategy and structure are then matched to the capability of the firm. When accepting strategic management, alignment and matching are important processes that firms need

to consider. To be able to break the ice there must be a working relation between strategy, structure and the environment (Johnson et al, 2008).

Structure is the design of the organization through which strategy is administered. Administrative problems can be caused due to changes in the organization's strategy. This will eventually cause a new structure to be formulated. The lines of reporting within an organizations and responsibilities best describe the structural design and influences the organizational growth. It is then important for organizations to ensure the structure in place support the strategy to ensure it does not undermine the overall goal (Johnson et al, 2008).

2.6 Empirical Studies and Knowledge Gaps

Several studies have been conducted on strategy and organizational structure. These studies have implication on both international and Kenyan economy which is evident with the established of Islamic windows within commercial banks and fully pledged Islamic banks. In the international context Miller, (2002) did a research on configuration between strategy and structure and found a strong configuration and relationship between strategy and structure through alignment and that strategy supports the structure in place. Al-ajlouni (2007) did a research on strategies used by Islamic banks to overcome future financial and globalization challenges in Malaysia and the study concluded that Islamic banks have to adapt to operational and globalization strategies for them to gain competitive advantage. Haron and Azmi (2005), did a research on Islamic banks marketing strategies and concluded that the strategies that attract and retain customers should be used.

According to Kavale, (2012) there is a direct connection between strategy and structure and it is the duty of top managers to ensure they are directly involved in developing the right structure that matches with the strategy in place. On the other hand structure has to change to better fit with the strategy and both are married to each other.

Issak & Kaswira (2012) studied the strategies that are used to achieve growth among banks that offer shariah compliant products and concluded that these financial institutions need to ensure there is strict following of shariah in their day to day operations. Mutua, (2012) further

established that strategy and structure alignment at Barclays bank was the reason for its success and those organizations that can obtain a fit between strategy and structure will increase their competitive edge and internal efficiency more effectively than those that didn't have. Mulandi, (2013) concluded that it's not necessary to change the structure of an organization every time there is a new strategy but it is important to have a strong structure in place to support the strategy. The study further established that every organization has unique strategy and structure that is different from other organization and this is due to the fact that every organization is faced with different environmental changes. The study recommended that organizational structure should be tested to know if it is able to support the strategies in place.

A study on Islamic strategy by Essajee, (2011) established the difficulty of implementing strategy at first community bank and concluded lack of knowledge, customer perception and few differentiations of products was the reason that their strategy was not successful. In another study Sheikh, (2009) established that the demand the Islamic banking products and the ever changing world trend was the strength to Islamic banking strategy. Past researches have concluded that there is a significant similarity that exists between Islamic banking strategy and organizational structure and it is through ensuring that the overall strategy fits with the structure (Gichohi, 2007).

Past researches have concluded that there is a direct correlation between strategy and the structure through proper implementation (Gichohi, 2007). Strategies lead to competitive advantage and according to Maa (1999), competitive advantage leads to superior returns. According to Jonsson & Devonish (2009) organizations that implement well thought out strategies tend to perform better than their rivals. Strategies that are competitive can lead to superior returns, satisfied clients and the ability to cope with rivals (Arasa& Githinji, 2014).

CHAPTER THREE: RESEARCH METHODOLOGY

This chapter discussed in details research design, population of study, sample size, data collection and data analysis techniques that were used for the purpose of this study. It provided systematic, theoretical analysis of the methods applied in the field that gave more insight to the area of study. It provided solutions to the area of study by providing better insight to the research work.

Research methodology is a systematic, theoretical analysis of the methods applied to the field of study. It entails the principles associated with the branch of knowledge and the body of methods. It encompasses concepts such as phrases, qualitative or quantitative techniques and such areas of study such as Islamic banking strategy and structure of Islamic commercial banks in Kenya (Irny and Rose, 2015).

The methodology is generally a research strategy that outlines the way in which research is to be undertaken and identifies the methods to be used in it. It defines the modes of data collection and specifies results to be calculated. A research methodology is a design process for carrying out research and collecting data (Irny and Rose, 2015).

3.2 Research Design

This is a plan that the researcher will use when conducting the research. It entails how the researcher will conduct the study through data collection, analysis and measurement. A research design is a framework that provides answers to research questions and provide methods to be used in collecting and analyzing the variables within the research problem (Kothari, 2014).

Descriptive census design was appropriate for this study because it guided the researcher in the process of collecting, analyzing and interpreting the data (Chavaand, 2005). Census enabled the researcher identify what managers considered to be the effect of Islamic banking strategy and structure of Islamic commercial banks in Kenya. It was through using census survey that reliable information was obtained that minimized biasness and was accurate in nature.

Descriptive research involves gathering data that describe events and then organizes, tabulates, depicts and describe the data collection (Glass & Hopkins, 1984). It often uses virtual aids such as graphs and charts to aid the reader in understanding the data distribution and therefore offer a better clarification on Islamic banking strategy and structure if Islamic commercial banks and ultimately give a clear picture on the effectiveness and reliability.

3.3 Population of the Study

A target population is the subset of the entire population on which the study will be carried out (Mugenda & Mugenda, 2003). The population that was targeted for this study was all banks in Kenya with Islamic window or fully Islamic compliant banks. The population selected provided ample information about Islamic banking strategy and structure of Islamic commercial banks in Kenya which in turn gave more information on strategy and structure alignment within an organization.

The population of this study was managers and shariah board involved in strategy and structure making within banks with Islamic windows or fully shariah compliant banks. There are six commercial banks in Kenya with Islamic windows and two fully shariah compliant banks. A census survey was used to collect information from the entire population.

The results of the population of the study helped the researcher in identifying the research gap that exist within Islamic commercial banks in Kenya and helped in analyzing the data. It also served as base to measure the dimensions of population and benefited the population that the research is done.

3.4Data Collection

This study adopted the use of primary data using both structured and semi structured questionnaires. Primary data is information that is obtained directly from the respondents (Kothari, 2004). Primary data is gathered at first hand following careful operationalisation of variables and using careful chosen procedures. It also has validity and is considered to be more trustworthy.

The study selected 3 senior managers and 2 middle level managers who included the branch managers, operational managers and business units' managers. The use of questionnaires as a method of collecting data made it easy collecting large amount of data within a limited time. The questionnaires were hand delivered and collected later. The questionnaire contained questions relating to organizational strategy, structure and the effect of Islamic banking strategy on organizational structure of commercial banks.

Secondary data was also collected from the banks overall vision plans, newsletters and other materials. Through the help of secondary data, it made primary data collection more specific since it was able to make out the gaps and deficiencies needed to be collected. It also provided a basis for comparison for collected data through understanding of the problem by the researcher.

3.5 Data Analysis

The data was analyzed using frequency distribution, standard deviation, mean score and percentage. A statistic package for social scientists (SPSS) was used in analyzing the data which was then interpreted using tables. A multiple regression model was used to determine the effect of Islamic banking strategy and structure of Islamic commercial banks using the following formulas:

$$Y = \beta_0 + \beta_1 \chi_1 + \beta_2 \chi_2 + \beta_3 \chi_3 + \epsilon$$

Where:

Y- is the dependant variable (Organizational structure

β_0 - is constant

$\beta_1 \chi_1$ - is the independent variable (Islamic bank strategy)

ϵ - is error term

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This section deals with the data that was collected on how Islamic banking strategy influences organizational structure of commercial banks in Kenya.

4.2 Response Rate

The sample size of this research was thirty respondents comprising of board members and managers of 6 commercial banks. Twenty six respondents fully participated and returned the questionnaire. This equals a response rate of 86.67%. According to Mugenda & Mugenda (1999), any rate above fifty percent is acceptable. The findings were presented in tables and charts.

4.3 Background Information

The first part of the study is on background information of the participants i.e. ownership of the organization, number of years bank has offered Islamic products and service, position hold in the organization, duration worked in the bank and age of the respondents. This was sought so as to understand the appropriateness of the participants in offering answers to the topic under study.

4.3.1 Ownership of the Bank

The participants were required to state the type of ownership for their organization. The results are shown in Table 4.3.1

Table 4.3.1 Ownership of the Bank

Ownership	Frequency	Percentage (%)
Foreign	4	66.67
Local	2	33.33
Total	6	100

Source: Researcher (2017)

From Table 4.3.1, we can conclude that 67% of the participants in the research were from foreign owned banks while the local owned respondents were 33%. This shows that the majority of the participants were from foreign owned bank. According to Abdi (2016) banks which are offering Islamic banks are mainly foreign owned banks with few local banks offering the same products. However, there is no fully local own Islamic banks indicating that local banks need to alter their organization structure so as to comply with Islamic banking products.

4.3.2 Number of Years Bank has been offering Islamic Products and Services

This researcher requested the respondents to indicate the number of years their bank has being offering Islamic products and services. The results are as shown in Table 4.3.2

Table 4.3.2 Number of Years Bank has been offering Islamic Products and Services

Number of years	Frequency	Percent (%)
4.00	3	11.5
5.00	2	7.7
6.00	5	19.2
9.00	16	61.5
Total	26	100.0

Source: Researcher (2017)

It was established that the majority of the banks have been offering Islamic products and services for nine years as shown by 61.5% (26) while 11.5% (3) revealed that their banks has been offering Islamic products and services in the last four years. It can be deduced that majority of the sampled banks have been offering Islamic banking products long enough and their input will be useful on the influence of Islamic banking strategy on organization structure.

4.3.3 Position Held in the Organization

The participants were required to demonstrate the positions they held in their companies. The results are as shown in Table 4.2.3

Table 4.3.3 Position Held in the Organization

Position	Frequency	Percent (%)
Managers	18	69.2
Board Members	8	30.8
Total	26	100

Source: Researcher (2017)

Majority of the respondents as shown in Table were managers as shown by 69.2% (18) while the board members were 30.8% (8). By having various managers and board members the study was able to gather information from the managerial position which is considered as decision making organ and where strategy are formulated. Therefore, these sampled respondents were able to give various input pertaining strategy formulation in relation to Islamic banking.

4.3.4 Duration Worked In the Bank

This researcher requested the respondents to indicate for how long they have worked for their respective companies. The results are as shown in Table 4.2.4

Table 4.3.4 Duration Worked In the Bank

Number of Years	Frequency	Percent (%)
1-5	3	11.5
6-10	7	27.0
Over 10 years	16	61.5
Total	26	100.0

Source: Researcher (2017)

It was established that the majority of the respondents' worked for the banks for a period of over 10 years with 61.5% while between 6 and 10 years were 26.92% (7) of the respondents. This allows them to have enough knowledge on the organizational structure of commercial banks as a

result of Islamic banking strategy. This confirms with Abdi (2016) who found that majority employees in Islamic banking section have been in their current position for more than 5 years.

4.3.5 Age of the Respondents

This researcher requested the respondents to indicate their age. The results are as shown in Table 4.3.5

Table 4.3.5 Age of the Respondents

Age	Frequency	Percent (%)
Between 20 years and 29 years	6	23.1
Between 30 years and 39 years	14	53.8
Between 40 years and 49 years	6	23.1
Total	26	100.0

Source: Researcher (2017)

Majority of the respondents were found to be between 30 and 39 years as shown by 53.8% of the sampled respondents. Between 20 and 29 years as well as between 40 and 49 years were 23.1% while none of the respondents were found to be over 50 years. It can be deduced that most of the respondents were young as indicated by 76.9% of the respondents who less than 40 years. The young age is associated with innovation and new ideas generations from conventional banking to diversification through Islamic banking. Mohamed (2013) indicated that young people at managerial level are risk taker in term of adopting various innovative strategies with aim of increasing company value.

4.4 Islamic Banking Strategy

The respondents were requested to rate how their bank measures its success in terms of the Islamic banking strategy in place. A five likert scale was used to place the answers from the participants with 5 representing strongly agree and 1 representing strongly disagree. An above 3 mean score is viewed as a satisfying measure of the test variables. Standard deviation (SD) demonstrates the variation or dispersion from the average. A standard deviation that is on the

lower side shows that the data points are closer to the mean. When the SD is high it shows that data is spread out over a large range of values. The results are as shown in Table 4.3,

Table 4.4 Islamic Banking Strategy

Islamic Banking Strategy	Mean	Standard Deviation
Growth	4.9	0.3
Profitability	4.9	0.4
Market share	4.5	0.5
Number of active accounts	4.5	0.5
Customer loyalty	4.7	0.4
Grand mean	4.7	

Source: Researcher (2017)

From Table 4.3 we can conclude that the participants agreed with aspects of bank measuring its success in terms of the Islamic banking strategy in place such as; Growth (M=4.9, SD=0.3); Profitability (Mean=4.9, SD=0.4); Market share (Mean=4.5, SD=0.5); Number of active accounts (Mean=4.5, SD=0.5) and Customer loyalty (Mean=4.7, SD=0.4). The overall mean of 4.7 implies that sampled banks measure its success in terms of the Islamic banking strategy in place at very great extent.

The findings suggest that Islamic banking strategy growth had highest impact from Islamic banking strategy and it was followed closely by profitability. Market share and number of active accounts though had very great extent but they had least measure of the five items. Islamic banking strategy introduces various products and services which attract new customers who were previous not covered due to their religious belief. The attraction of new customers results to growth in opening of new branches that would serve this kind of customers. Further, this increases market share through active accounts.

4.5 The Strategy Adopted and Implemented

The respondents were requested to state the extent of their agreement that the strategy adopted and implemented has helped the organization achieve its goals. A 5 likert scale was used to place

the answers from the participants with 5 representing Very large extent and 1 representing not at all. An above 3 mean score is viewed as a satisfying measure of the test variables. Standard deviation (SD) demonstrates the variation or dispersion from the average. A standard deviation that is on the lower side shows that the data points are closer to the mean. When the SD is high it shows that data is spread out over a large range of values. Table 4.5 shows a summary of the results.

Table 4.5 Strategy Adopted and Implemented

Name of strategy type	Mean	Standard Deviation
Cost leadership	4.5	0.6
Price leadership	4.4	0.8
Product differentiation	4.4	0.7
Market and Sales differentiation	4.7	0.6
Emulation of conventional products	4.6	0.6
Reputation of the bank	4.4	0.6
Mean	4.5	

Source: Researcher (2017)

From Table 4.4 it can be deduced that there was large extent in the adoption and implementation such as Cost leadership (Mean=4.5, SD=0.6); Price leadership (Mean=4.4, SD=0.8); Product differentiation (Mean=4.4, SD=0.7) and Reputation of the bank (Mean=4.4, SD=0.6). It was revealed that there was very large extent in the adoption and implementation such as Market and Sales differentiation (Mean=4.7, SD=0.6) and Emulation of conventional products (Mean=4.6, SD=0.6). An overall mean of 4.5 implies that Strategy Adopted and Implemented has very greatly helped the organization achieve its goals. Market and sales differentiation has the greatest impact since Islamic banking products offers varieties which bring in more customers who are willing to sample them. This is closely followed by emulation of conventional products by offering products that the customers want apart from the Islamic banking products. Reputation of the bank, product differentiation, price leadership and cost leadership have the list impact because all commercial banks by the CBK.

The respondents were further asked to state how often the strategies are reviewed. The results are as shown in Table Below,

Table 4.5.1 How often Strategies are reviewed

How often strategies are reviewed	Frequency	Percent (%)
Between 1year and 3years	2	7.4
Between 3 years and 5years	3	11.1
Between 5years and 10years	20	74.1
10years and above	1	3.8
Total	26	100.0

Source: Researcher (2017)

From the above figure, majority of the respondents indicated that they reviewed their strategies between 5 and 10 years as shown by 74.1% (20) of the respondents. However, 7.4% (2) indicated they reviewed it regularly between 1 and 3 years. Most banks argued that it was a costly affair to review their strategies year after year and preferred to review it on a period between 5 and 10 years.

4.6 Factors that led to the adaptation of Islamic banking strategy

The respondents were requested to state the extent of factors that led to the adaptation of Islamic banking strategy. A five likert scale was used to place the answers from the participants with 5 representing strongly agree and 1 representing strongly disagree. An above 3 mean score is viewed as a satisfying agreement of the test variables. Standard deviation (SD) demonstrates the variation or dispersion from the average. A standard deviation that is on the lower side shows that the data points are closer to the mean. When the SD is high it shows that data is spread out over a large range of values. Table 4.6 shows a summary of the results.

Table 4.6 Factors that led to the adaptation of Islamic banking strategy

Adaptation Of Islamic Banking Strategy	Mean	Standard Deviation
Increased competition in the market	1.4	0.7
High expectation of return to shareholders	1.3	0.7
Market demand for Islamic products	1.3	0.6
Worldwide trend and expectations	1.5	0.6
Direct response to competitors plan	1.3	0.6
Need for diversification	1.4	0.6
Need for focus	1.0	0.1
As experimental products	4.7	0.6

Source: Researcher (2017)

On a scale of 1 to 5 where one was strongly disagree and 5 was strongly agree, the mean was calculated at 1.4074 for respondents who felt that the increased competition in the market has led to the adaptation of Islamic banking strategy. This indicated that respondents strongly disagree that increased competition in the market has contributed to adoption and implementation. Similar results were obtained for High expectation of return to shareholders (Mean=1.3, SD=0.7); Market demand for Islamic products (Mean=1.3, SD=0.6); Worldwide trend and expectations (Mean=1.5, SD=0.6); Direct response to competitors plan (Mean=1.3, SD=0.6); Need for diversification (Mean=1.4, SD=0.6) and Need for focus (Mean=1.0, SD=0.2). However, the mean for experimental products was calculated at 4.7 for respondents who felt that the experimental products have led to the adaptation of Islamic banking strategy. This indicated that respondents strongly agree that experimental products in the market have led to adoption and implementation. Every commercial bank with Islamic windows or fully shariah compliant work towards gaining competitive advantage over the rivals and its through experimental products that they are able to go an extra mile.

4.6 Islamic Banking Structure

The respondents confirmed that the structure of commercial banks with Islamic windows and fully shariah compliant are governed by shariah boards and advisory boards and are demonstrated in the following:

4.6.1 Elements of Islamic Banking Structure

Respondents were asked how else their organization has adopted Islamic banking strategy to enhance the structure of commercial bank. It was found that banks have established shariah advisory board to ensure strict shariah compliance. The bank has put in place shariah training for staff on monthly basis.

Bank officials including Shari'ah Boards were required to state the elements that have to be considered to ensure proper Shari'ah compliance. They included Shari'a Board membership and Qualifications, Shari'a Board meetings, Shari'a Board's relationships, Information available to Shari'a Boards, Shari'a Board annual report, Internal Shari'a Control membership and Qualifications, Rules and procedures of Shari'a control, Reports of Shari'a control, Information available to Shari'a control, Violations and mistakes dealt with by Shari'a control, Payment and treatment of Zakah, Accounting regulations, Social image and objectives, Training and human resources, Modes of financing, Distribution of income and Social environment within the institution. This shows that for a structure to be properly governed it has to be well managed through shariah board compliance with will influence the overall performance.

4.6.2 Special training on Islamic Finance Operations

All of the respondents confirmed that they went for a special training on Islamic Finance Operations. The researcher further sought to find out who conducts these trainings

Table 4.6.1 Special training on Islamic Finance Operations

Special training on Islamic finance operations	Frequency	Percentage (%)
Internal trainers	22	85.2
External trainers	19	74.1
Shari'ah Board	21	81.5

Source: Researcher (2017)

The results show that the internal trainers mostly conducted training as shown by 85.2% of the respondents while Shariah Board were identified by 81.5% of the respondents and 74.1% identified external trainers who undertook training in the sampled banks. This goes to show that most commercial banks preferred doing internal training because its much cheaper and convenient compared to external training.

Table 4.6.2 Shariah Boards

Shariah Boards	Frequency	Percentage (%)
Shariah Board	23	85.2
Shariah supervisor	22	81.5
Internal Shariah Auditor/ Shariah control department	20	74.1
External Shariah Auditor	21	77.8

Source: Researcher (2017)

From Table 4.6.2, majority of the respondents indicated they have Shariah Board as shown by 85.3% of the respondents and Shariah supervisor as shown by 81.5% of the respondents. The results further revealed that 74.1% had internal Shariah Auditor/ Shariah control department and 77.8% had External Shariah Auditor. This shows the importance of establishing the shariah board who are incharge of guidance towards better performance of the Islamic windows.

The respondents were further required to state if there been any Shariah compliance issue raised by their internal regulators in the time their bank has been in operation. The results are as shown in Table below.

Table 4.6.3 Shariah compliance issues raised

Response	Frequency	Percent (%)
Yes	5	18.5
No	22	81.5
Total	27	100.0

Source: Researcher (2017)

From above Table, majority of the respondents indicated that there has been no Shariah compliance issue raised by their internal regulators in the time their bank has been in operation as shown by 81.5% of the respondents.

The respondents were further asked to rate how their bank has established accounting and auditing standards according to Islamic shariah. The extent of their agreement ranged from 1 to 5

where 5-Strongly Agree, 4-Agree, 3-Neutral, 2-Disagree and 1-Strongly Disagree. The findings are as shown in Table below

Table 4.6.4 Rate of Establishment of Accounting and Auditing Standards

Accounting And Auditing Standards	Mean	Standard Deviation
Creation of Islamic accounting rules	4.7	0.7
Creation of accounting standard body	1.1	0.4
Pursuing harmonization of shariah based rules across jurisdictions	1.3	0.5
Training on standard of regulators and financial institutions	1.3	0.7
Testing of accounting and auditing conventions	1.3	0.5
Ensuring consistency in Islamic accounting standards	1.2	0.4

Source: Researcher (2017)

From Table above, it was strongly agreed that there is creation of Islamic accounting rules as shown by mean 4.7 and standard deviation 0.7. Similarly, it was strongly disagreed that there is creation of accounting standard body as shown by mean of 1.1 and standard deviation of 0.4. The respondents also strongly disagreed that they are pursuing harmonization of shariah based rules across jurisdictions, training of standard of regulators, testing of accounting and auditing (Mean=1.3) and finally respondents strongly agreed that they ensure consistency in Islamic accounting standards (Mean=1.2, SD=0.4). This shows that through creation of accounting rules highly contributed to establishment of accounting standards.

4.7 Chi-Square Analysis between Islamic banking Strategy and Structure

Chi square tests of independence were used for testing associations between dependent variable (Organization Structure) and independent variables (Islamic Banking Strategy) at significance level of 0.05. Cramer's V was provided to indicate effect size for Chi square tests. Cramer's V is the square root of chi-squared divided by its minimum possible value and measures the strength of association between the variables in the chi-square test. Cramer's V of less than 0.20 is

generally considered a weak relationship, 0.20-0.49 is considered moderate relationship and with a value of more than 0.49 is considered a strong relationship.

4.7.1 Shariah Board

Pearson Chi-Square of association was conducted to find the Islamic banking strategy affected organization structure. The relationship between Shari'ah board and high expectation of return to shareholders and direct response to competitors plan was investigated. The results are as shown in Table below.

Table 4.7.1 Shariah Board

	Value	df	Asymp. Sig. (2-sided)
Shari'ah Board and High expectation of return to shareholders			
Pearson Chi-Square	8.460 ^a	2	.015
Cramer's V	.570		.015
N of Valid Cases	26		
Shari'ah Board and Direct response to competitors plan			
Pearson Chi-Square	12.831 ^a	2	.002
Cramer's V	.703		.002
N of Valid Cases	26		

Source: Researcher (2017)

The results displayed in Table above show that there was statistically significant association between shariah board and High expectation of return to shareholders ($P=0.015$) as well as direct response to competitors plan ($P=0.002$). This implies that formation of shariah board in the sampled banks have been influenced strategies related with High expectation of return to shareholders and Direct response to competitors plan.

4.7.2 Shari'ah supervisor

Pearson Chi-Square of association was conducted to find the Islamic business strategy affected organization structure. The relationship between Shari'ah supervisor and Reputation of the bank, increased competition in the market and Islamic banking strategy was investigated. The results are as shown in Table below.

Table 4.7.2 Shari'ah supervisor

	Value	df	Asymp. Sig. (2-sided)
Shari'ah supervisor and Reputation of the bank			
Pearson Chi-Square	8.442 ^a	2	.015
Cramer's V	.570		.013
N of Valid Cases	26		
Shari'ah supervisor and Increased competition in the market			
Pearson Chi-Square	10.780 ^a	2	.005
Cramer's V	.644		.013
N of Valid Cases	26		

Source: Researcher (2017)

The results displayed in Table above show that there was statistically significant association between Shari'ah supervisor and Reputation of the bank ($P=0.015$) as well as increased competition in the market ($P=0.005$). This suggests that formation of shariah supervisor in the sampled banks have been influenced reputation of the bank and increased competition in the market.

4.7.3 Internal Shari'ah Auditor/ Shari'ah control department

Pearson Chi-Square of association was conducted to find the Islamic business strategy affected organization structure. The relationship between internal Shari'ah auditor/ Shari'ah control department and product differentiation as well as high expectation of return to shareholders was investigated. The results are as shown in Table below.

Table 4.7.3 Internal Shari'ah Auditor/ Shari'ah control department

	Value	df	Asymp. Sig. (2-sided)
Internal Shari'ah Auditor/ Shari'ah control department and Product differentiation			
Pearson Chi-Square	10.207 ^a	2	.006
Cramer's V	.627		.013
N of Valid Cases	26		
internal Shari'ah Auditor/ Shari'ah control department and High expectation of return to shareholders			

Pearson Chi-Square	11.635 ^a	2	.003
Cramer's V	.669		.013
N of Valid Cases	26		

Source: Researcher (2017)

The results displayed in Table above show that there was statistically significant association between Internal Shari'ah Auditor/ Shari'ah control department and Product differentiation ($P=0.006$) as well as High expectation of return to shareholders ($P=0.003$). This suggests that formation of Internal Shari'ah Auditor/ Shari'ah control department is as a result of adopting Product differentiation strategy and High expectation of return to shareholders

4.7.4 External Shari'ah Auditor

Pearson Chi-Square of association was conducted to find the Islamic business strategy affected organization structure. The relationship between External Shari'ah Auditor and market share as well as high expectation of return to shareholders was investigated. The results are as shown in Table below.

Table 4.7.4 External Shari'ah Auditor

	Value	df	Asymp. Sig. (2-sided)
External Shari'ah Auditor Market share			
Pearson Chi-Square	15.758 ^a	1	.000
Cramer's V	.778		.000
N of Valid Cases	26		
External Shari'ah Auditor and Market and Sales differentiation			
Pearson Chi-Square	12.051 ^a	2	.002
Cramer's V	.681		.002
N of Valid Cases	26		

Source: Researcher (2017)

The results displayed in Table above show that there was statistically significant association between External Shari'ah Auditor and market share ($P=0.000$) as well as increased Market and Sales differentiation ($P=0.002$). This suggests that external shariah auditor in the organization structure is influenced by strategy related to profitability, market and sales differentiation.

From the Pearson Chi-square of association, strategy adopted and implemented by sampled banks such as market and sales differentiation, product differentiation and reputation of the bank influenced the organization structure significantly. Factors that led to the adaptation of Islamic banking strategy such as High expectation of return to shareholders, direct response to competitors plan, and increased competition in the market also influenced the organization structure of sampled banks. Lastly, market share which was Islamic banking strategy was also found to influence sampled Islamic banks organization structure.

4.8 Discussion of the Findings

The findings have revealed that Islamic banking strategy is associated with various performance indicators which are both financial and non-financial. The aim of conventional banks is to satisfy shareholders through profits and share value. They adopt a particular strategy that would enhance shareholder value. However, the aim of Islamic banks is to socially empower the society through various financial products even though the banks may have dual objectives. Even though they can emulate conventional bank financial products, they should not drift from their social mission. Therefore, it is expected that banking strategy adopted by Islamic banks should be different from conventional banks. Customer loyalty, cost leadership, price leadership, product differentiation and reputation should inform Islamic banking strategy. These findings agree with Issak & Kaswira (2012) who found out that commercial banks have achieved growth due offer shariah compliant products. Further, Mutua (2012) also revealed that strategy and structure alignment at Barclays bank was the reason for its success and those organizations that can obtain a fit between strategy and structure will increase their competitive edge and internal efficiency more effectively than those that didn't have.

Shariah Compliance Regulations was examined based on board membership, Rules and procedures of Shari'ah control, Training and human resources among other parameters. It was confirmed that majority of the banks have created Islamic accounting rules according to Islamic shariah. However, there was disagreement as far ensuring consistency in Islamic accounting standards, testing of accounting and auditing conventions, training on standard of regulators and financial institutions, pursuing harmonization of shariah based rules across jurisdictions and creation of accounting standard body is concerned. This is consistent with Mulandi, (2013)

concluded that it is not necessary to change the structure of an organization every time there is a new strategy but it is important to have a strong and dynamic structure in place to support organization strategy. Essajee, (2011) also concluded that it is difficult to implement strategy at first community bank and concluded lack of knowledge, customer perception and few differentiations of products was the reason that their strategy was not successful.

Finally the results did prove that there is significant relationship between Islamic banking strategy and organization structure. It was found that at significance level of 0.05. Cramer's V of the changes in organizational structure of commercial banks are significantly accounted for by Islamic banking strategy through factors that led to the adaptation of Islamic banking strategy such as High expectation of return to shareholders, direct response to competitors plan and increased competition in the market. This implies that Islamic strategy cannot be ignored in both commercial banks offering Islamic products as well as Islamic banks in Kenya. Most of conventional commercial banks have altered their organization structure to accommodate Islamic customers which are significant market in Kenya. This can only be achieved by adopting Islamic banking strategy which is dominant in countries where Muslims are majority. Therefore, Islamic banking strategy significantly influences organization structure. Past researches have concluded that there is a significant similarity that exists between Islamic banking strategy and organizational structure and it is through ensuring that the overall strategy fits with the structure (Gichohi, 2007).

CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary of findings, conclusion of the study, recommendations for policy and practice, limitations of the study, and suggestions for further research. The main objective of this study was to determine how Islamic banking strategy influences organizational structure of commercial bank in Kenya.

5.2 Summary

The study sought to determine how Islamic banking strategy influences organizational structure of commercial banks in Kenya. The major findings are summarized as follows.

Majority of the sampled Islamic banks were foreign owned and they were offering Islamic products and services for the last nine years. Majority of the workers have been working in the bank for the last 12 years therefore they were in position to offer their views and opinion in Islamic banking. Majority of the sampled respondent were between 30 and 39 years old.

Most of the banks have been offering Islamic banking products for a long time with majority been above 9 years and therefore were able to point out the changes that has taken place in the strategy and organizational structure in the past years and how they influence each other. A significant number of respondents were managers and a few board members which is significant in establishing how decision making process and strategy were formulated.

Majority of the respondents strongly agreed that bank growth and profitability is associated with success of Islamic banking strategy. Similar results were obtained for market share, number of active accounts and customer loyalty. The results further revealed that strategy adopted and implemented such as Market and Sales differentiation and Emulation of conventional products has help the organization to achieve their objective at very great extent while Cost leadership,

Price leadership, Product differentiation and Reputation of the bank at great extent. The strategies were found to be reviewed between 5 and 10 years.

Factors that led to adoption of Islamic banking strategy were found to be as experimental products. However, majority of the respondents strongly disagree that increased competition in the market, high expectation of return to shareholders, market demand for Islamic products, worldwide trend and expectations, direct response to competitors plan, need for diversification and need for focus were among the factors that led them to adoption of Islamic banking.

Shariah Compliance Regulations was examined based on board membership, Rules and procedures of Shari'ah control, Training and human resources among other parameters. All of the respondents confirmed that they went for shariah and special training on Islamic Finance Operations which was mostly conducted by internal trainers. Other received their training from external trainers and shariah board.

The results revealed they have shariah board and shariah supervisor which aided in the Islamic banking operations. There was also Internal Shariah Auditor/ Shariah control department and external shariah auditor which were found to be fundamental in the implementation. In this regard there was no Shariah compliance issue raised by their internal regulators in the time their bank has been in operation. It was confirmed that majority of the banks have created Islamic accounting rules according to Islamic shariah. However, there was disagreement as far ensuring consistency in Islamic accounting standards, testing of accounting and auditing conventions, training on standard of regulators and financial institutions, pursuing harmonization of shariah based rules across jurisdictions and creation of accounting standard body is concerned.

Chi square tests of independence were used for testing associations between dependent variable (Organization Structure) and independent variables (Islamic Banking Strategy) at significance level of 0.05. Where it was found that formation of shariah board influenced strategies in the sampled banks related with High expectation influenced return to shareholders. It was also found that the relationship between Shari'ah supervisor and Reputation of the bank increased competition in the market and Islamic banking strategy. The formation of shariah supervisor in

the sampled banks have been influenced reputation of the bank and increased competition in the market.

5.3 Conclusions

Basing on the found, it was concluded that majority of the banks offering Islamic products and services are foreign owned and they have been offering these products and services for the past 9 years. This indicates that organization structure of the sampled commercial banks have been influenced by Islamic banking strategy and foreign ownership organization culture.

It is also concluded that Islamic banking strategy has great influence on organization success through their growth, profitability, market share, number of active accounts and customer loyalty. This implies that banks that have adopted and implemented Islamic banking strategy derive their success both financially and none financially which contribute to organization success.

The study concluded that these commercial banks have adopted various strategies to help achieve organizational goals. The strategies were meant to achieve competitive advantage, social entrepreneurship and financial performance. The review of these strategies was done between 5 and 10years. Most of these strategies were found to be differentiation strategies such as product, market and sales differentiation. There was also emulation of conventional products to Islamic products and services which increases the competitiveness of the commercial banks in the market.

Although there are various factors that lead to the adaption of Islamic banking strategy, it was found that all the adopted used Islamic products and services as experimental products unlike competition in the market, financial expectation, market demands and desire for diversification.

On Shariah Compliance Regulations, it was concluded that banks have established shariah advisory board to ensure strict shariah compliance. This was revealed through internal audit, special training on Islamic finance operations, shariah board, shariah supervisor, internal shariah auditor/ shariah control department and external shariah auditor. These ensured that there was no

any Shariah compliance issue raised by their internal regulators in the time their bank has been in operation.

The study also concluded that there was creation of Islamic accounting rules as far as accounting and auditing standards are concerns. However, there was no creation of accounting standard body, testing of accounting and auditing conventions and training on standard of regulators and financial institutions. Lastly the study concluded that organizational structure is significantly influenced by Islamic banking strategy.

5.4 Recommendations

The findings have revealed that Islamic banking strategy has led to success in growth, profitability, and market share and customer loyalty. The following recommendation were made base on the study conclusions.

Islamic banks as well as the commercial banks offering Islamic products and services should review their strategies regularly within less than five years so that they are able to meet market and organization demand in offering of Islamic products and services. This can be achieved regular monitoring and evaluation as well as market research involving both Islamic and non-Islamic customers.

The main factor that led to adoption of Islamic banking strategy is experimental products. This implies that other factors are not put into consideration when formulating strategy for Islamic banking. It is recommended that Islamic banks should analyze the market before coming up with strategies. Islamic banks should adopt effective competitive strategies to align with the changing business environment. Islamic banks should adopt focus strategies to counter competition. Islamic bank products should be unique from their competitors. Islamic banks should be proactive in adopting competitive strategies in response to competitors plan

Islamic banks should adopt sales strategies that work for them. Islamic banks should align sales strategies with organization goals. Islamic banks should asses the marketing strategies effectiveness by coming up with quantitative characteristics which can be obtained from an

Islamic banks sample. Islamic banks should change their sales strategies according to the changing business environment.

Islamic banks should develop clear guidelines on their shariah compliance regulations. The guidelines and regulation should help banks in understanding the types of expectations so as to appreciate benefits customers expect to receive. The formulation of regulation should include Shariah Board, Shariah supervisor, Internal Shariah Auditor/ Shariah control department and External Shariah Auditor. These regulations should be aimed in delivering quality Islamic products and services thereby increasing the number of customers.

Conventional banking system and operational mechanism needs to be re-examined. It should then be converted into PLS system as a policy mechanism considering beneficial impact of the economy to come later in the days. For Islamic banks are to operate successfully within the framework of conventional banking framework, it is important to consider the recommendations of the heads in place.

There is need of constant special training on Islamic finance operations provided by internal trainers, external trainers and shariah board. This can be done by drafting training framework that would include three actors simultaneously. The inclusion of external trainers would ensure that market regulations are adhered to.

A legislative framework should be put in place to enhance the regulation of the industry. This means both the Central Bank Act as well as Banking Act should be amended to incorporate Islamic Banking concepts. This would ensure that there is consistency in Islamic accounting standards.

Further, its recommended that a National Shari'ah Supervisory Board should be constituted to guide a process of Itihad led standardization and convergence of products, set qualification and certification of Banks' Shari'ah Board members and set rules for Shari'ah control. This would ensure there is harmonization of shariah based rules across jurisdictions

Lastly, as far as accounting and auditing standards according to Islamic shariah is concerned, the study strongly recommends that training on standard of regulators and financial institutions

should be implemented by all stakeholders in Islamic banking. This would ensure there is maximum compliance on shariah regulations.

5.5 Study Limitations

Due to the sensitivity of the information in the banks, the respondents were very careful on the information they were sharing out with the researcher during the study especially Islamic banking which is closely related with religion. In this worry the researcher conquered this issue by giving the letter of research to demonstrate that she is a master student and that the data gathered is for scholarly purposes.

The number of Islamic banks offering shariah compliant products is still young in the banking industry and need most time to establish them fully in the industry. This provided a sample size which reduces variability of data during both descriptive and regression analysis. This was overcome by ensuring there is high response rate of over 80% so as variability is achieved.

The study required a lot of input from top executives and board members who are involved with making decisions on the Islamic banking strategy. However, their availability was very limited due to the nature of their status and job requirement. This provided a lot of challenges in the study since the researcher had to make several trips of postponed appointments. Nevertheless, the study was able to achieve over 80.0% of response rate despite this limitation.

5.6 Suggestion for further studies

The study was carried in Islamic banks and commercial banks offering Islamic products and services. It is very difficult for Islamic banking strategy to influence conventional banks which are offering Islamic products and services. Therefore future studies should focus on pure Islamic banks for generalization of the findings.

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APPENDIX 1: QUESTIONNAIRE

This research will be undertaken with the aim of understanding the effect of Islamic banking strategy on structure of commercial banks. Any information received from you will be dealt with the highest level of confidentiality and will be used for academic reasons only.

PART ONE: BACKGROUND INFORMATION

Name of organization _____

What is the ownership of the organization?

Foreign () Local () Both ()

How many years has your bank offered Islamic products and service?

What position do you hold in the organization?

Name of the bank?

Name of branch?

How long have you worked for the bank?

What age bracket do you fall under? (Please tick (Π) in ONE of the boxes provided below).

- | | |
|----------------------------------|-----|
| a. Less than 20 years | [] |
| b. Between 20 years and 29 years | [] |
| c. Between 30 years and 39 years | [] |
| d. Between 40 years and 49 years | [] |
| e. 50 years and above | [] |

PART TWO: ISLAMIC BANKING STRATEGY

Rate how your bank measures its success in terms of the Islamic banking strategy in place?

	Strongly agree	Agree	Neutral	Disagree	Strongly Disagree
Growth					
Profitability					
Market share					
Number of active accounts					
Customer loyalty					

Would you agree that the strategy adopted and implemented has helped the organization achieve its goals?

Name of strategy type	Not at all	Little extent	Fair extent	Large extent	Very large extent
Cost leadership					
Price leadership					
Product differentiation					

Market and Sales differentiation					
Emulation of conventional products					
Reputation of the bank					

How often are the strategies reviewed?

- a. Less than an year ☐
- b. Between 1year and 3years ☐
- c. Between 3 years and 5years ☐
- d. Between 5years and 10years ☐
- e. 10years and above ☐

Factors that led to the adaptation of Islamic banking strategy

	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
Increased competition in the market					
High expectation of return to shareholders					
Market demand for Islamic products					

Worldwide trend and expectations					
Direct response to competitors plan					
Need for diversification					
Need for focus					
As experimental products					
Others (Specify).....					

How else has your organization adopted Islamic banking strategy to enhance the structure of commercial

bank?.....
.....
.....
.....

PART THREE: SHARI'AH COMPLIANCE REGULATIONS ON STRUCTURE

(To be completed by respondents who are Bank officials including Shari'ah Boards)

(The elements that have to be considered to ensure proper Shari'ah compliance include:

Shari'a Board membership and Qualifications

Shari'a Board meetings

Shari'a Board's relationships

Information available to Shari'a Boards

Shari'a Board annual report
Internal Shari'a Control membership and Qualifications
Rules and procedures of Shari'a control
Reports of Shari'a control
Information available to Shari'a control
Violations and mistakes dealt with by Shari'a control
Payment and treatment of Zakah
Accounting regulations
Social image and objectives
Training and human resources
Modes of financing
Distribution of income
Social environment within the institution
Other considerations

1.0. Did you go for a special training on Islamic Finance Operations?

YES []

NO []

1.1. Who conducts these trainings?

Internal trainers []

External trainers []

Shari'ah Board []

2.0. Does your institution have a Shari'ah Board?

YES []

NO []

2.1 Does your institution have a Shari'ah supervisor?

YES []

NO []

2.2 Does your institution have an internal Shari'ah Auditor/ Shari'ah control department?

YES []

NO []

2.2 Does your institution have an external Shari'ah Auditor?

YES []

NO []

2.3 Has there been any Shari'ah compliance issue raised by your internal regulators in the time your bank has been in operation?

YES []

NO []

If YES which ones:.....

.....

.....

B. ACCOUNTING AND AUDITING STANDARDS

Rate how has your bank established accounting and auditing standards according to Islamic shariah?

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree

Creation of Islamic accounting rules					
Creation of accounting standard body					
Pursuing harmonization of shariah based rules across jurisdictions					
Training on standard of regulators and financial institutions					
Testing of accounting and auditing conventions					
Ensuring consistency in Islamic accounting standards					

THANK YOU

APPENDIX 2: LIST OF ISLAMIC COMMERCIAL BANKS

Barclays Bank

KCB Bank

National Bank

Standard Chartered Bank

Gulf African Bank

First Community Bank