RESPONSES BY AAR CREDIT SERVICES LTD TO CHANGES IN THE ENVIRONMENT

BY

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DECLARATION

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

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

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DEDICATION

To Mum and Dad for your love and encouragement this project is affectionately dedicated.

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Special appreciation to the following for their invaluable input to this project.

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ABSTRACT

Liberalisation and globalisation of world economies have caused turbulence in the business environment. Hitherto protected organisations have found themselves in an unfamiliar trading environment. Their past operational inefficiency and markets are no longer protected. They are now under pressure to change and align their structures and management strategies to the changes in the environment.

The study was to ascertain the responses by AAR Credit Services Ltd to changes in the environment. Its objective was to document the challenges caused by these changes and AAR Credit Services' response to them.

The study was conducted by carrying out in-depth interviews with the Managing Director and also with the five staff of AAR Credit Services Ltd. An interview guide was used to facilitate the data collection processes. The interview guide had open-ended questions.

The findings confirmed that the company operates in an environment that is not static but is characterized by many changes and challenges. These challenges include competition, poor economic environment and changes in technology.

The study established several responses by AAR Credit Services to the changes in the business environment it operates in. New products as part of AAR Credit Services diversification plans have been launched to cater for different income groups. AAR Credit Services has also entered into business partnerships with several Blue-chip companies to offer various products to the existing AAR customers and also to other target groups. AAR Credit Services continues to enhance its information technology with a view to increasing efficiencies in its operations.

AAR Credit Services has to respond to the changes and challenges it is facing in the external environment. It must continually re-invent itself as its strategies are copied by its

competitors with time. AAR Credit Services hopes to improve its service delivery and develop a wider range of products.

The study recognizes that AAR Credit Services is a non-banking institution that has continued to be profitable in a competitive finance market and it recommends that a study should be carried out to find out the responses by other institutions to changes in the environment.

CHAPTER ONE: INTRODUCTION

1.1 BACKGROUND

1.1.1 THE BUSINESS ENVIRONMENT

The business environment can be relatively stable or turbulent. Each level of turbulence has different characteristics and requires a different strategy to match. The strategy in-turn has to be matched by appropriate organisational capability for survival, growth and development (Ansoff and McDonnell, 1990). In a stable environment organisations are under no pressure to change. The major concern then is maintaining the firm's position against any competition. Turbulence in the business environment puts pressure on organisation to change so they can effectively sustain their competitive advantage (Worley et al, 1996). To be able to retain competitive advantage organisations need to examine their environment both internal and external and respond accordingly (Porter, 1985).

Turbulence in the global business environment affects all organisations that operate within its boundaries. Organisations being environment dependent have to consistently adapt their activities and internal configurations to reflect the new external realities and failure to do this may put the future success of an organisation in jeopardy (Aosa, 1998). Porter (1985) argues that the origin of competitive advantage maybe found in a firm's local environment. Organisations are required to have a profound understanding of the industry they are in. This requires them to have a thorough knowledge of the critical success factors and the drivers of changes in the industry. An organisation can further compete effectively when it identifies the strategic group it belongs to within the industry and therefore learn more about its closest rivals and the intra-industry success factors and to develop focused strategies that will enable it occupy alternative segments (Whipp and Pettigrew, 1993).

Fundamental forces of change have been experienced in the global business environment resulting in unprecedented competition. Organisations responding to these changes have realised their existing strategies and configurations may no longer serve them well (Ansoff & McDonnell, 1990). An organisation's external environment is one of constant change. Both the degree of change and the rate of change are important factors, and determine whether an organisation's external environment is relatively stable or unstable. External environmental factors most responsible for change include competition, culture, customers, politics, technology, and the labour force. Individuals in organisations must often make decisions under conditions of risk and uncertainty. These decisions reflect the environmental forces that those individuals cannot control, but that may in the future influence the outcomes of their decisions.

It is imperative that managers apply critical investigations into the realities of the changing environment of this millennium through enlightened diagnosis of the problem it poses. Political, environmental, social and technical factors, for example, can influence the lifestyle and the health of people. This same environment should also be seen as a system that calls for profound understanding in order to improve decision making and recognise the links between the past, present and future and also between local and global matters. This necessitates that strategic managers view the environment in its entire context and perspective in order to understand the concept of strategic management (Ansoff & McDonnell, 1990).

1.1.2 THE PREMIUM FINANCE MARKET

The Kenyan business environment is not exempt from what the global scenes are experiencing. In the Kenyan economy, in the last ten years, the service sector has grown dramatically e.g. the growth of the telecommunication industry, health maintenance organizations (HMOs), garbage collection services, foreign exchange bureaus, and so on, while the product sector has shrunk (Kimonye, 1998). The Kenyan environment is changing rapidly. Given these fundamental changes in Kenya we would expect organisations operating in Kenya to change.

Managed care refers to a model of health care in which services are provided to members of a health care plan in a coordinated manner designed to promote increased quality of care and cost control. Managed care has come to replace traditional fee-for-service programs as the dominant way of providing health care services. In Kenya, as in the rest of the world, one of the dominant types of managed care organizations are health maintenance organizations (HMOs). Health maintenance organizations (HMOs) are health plans that contract with medical groups to provide a full range of health services for their enrollees for a fixed pre-paid, per-member fee. Traditional fee-for-service insurance is a health insurance plan that reimburses physicians and hospitals for each individual service provided. These plans allow consumers to choose any physician or hospital that they prefer.

In Kenya, AAR Health Services Ltd is an HMO that continues to remain the dominant player in the market for pre-paid medical services. Its turnover for the financial year ending 30 April 2004 exceeded Kshs 1 billion. Seventy five percent of this business is from corporate members. Currently AAR Credit finances approximately 25% of AAR membership subscriptions. AAR Health Services has a membership base of 75,000 in Kenya alone. This is however only a small fraction of its estimated target market size of 2.5 million individuals consisting of employees and their dependants in major urban centres. Financing pre-paid health care subscriptions therefore has a tremendous growth potential. The other HMOs in Kenya include Avenue Health Ltd, Prosperity Health Ltd and Resolution Health Ltd. AAR Credit Services Ltd however only finances the membership subscriptions of AAR Health Services Ltd currently.

The premium financing market is specialised. It is clearly similar to personal lending. Whether commercial or consumer based, deals are short lived as the maximum lending period is limited to 12 months, the duration of the insurance policy and volumes are high. Typically heavily reliant on a network of brokers for source of business, automation and connectivity are the keys to efficient processing of the business. Pushing functionality to your partners will reduce costs associated with deal processing and increase data quality, thus raising margins and delivering a better quality of service to your partners.

AAR Credit Services Ltd has worked with its premium financing customers to extend the functional breadth of the product. Key processes and deal attributes, particular to this market sector, are supported in such a way as to deliver to the same set of objectives for any other – adding value through automation and accuracy. The competition in the insurance industry is very intense, as there are currently 38 insurance companies in Kenya with the numbers steadily rising over the years. In price competition, companies compete on the basis of price by affording a lower priced product than other companies dealing in the same line of insurance. In quality competition, companies compete by offering different forms of policies with additional products beneficial to the consumer. Companies also compete on service where insurance companies who give good service enjoy competitive advantage since insurance is a promise of future performance. Some insurance companies give free gifts items in addition to the service for example umbrellas and T-shirts (College of Insurance, 2000).

All Insurance companies use the same sales agents especially the brokers and agencies. The difference comes in the use of direct sales agents who are tied to the company. The company that invests in the direct sales force and develops motivational programs to retain the sales people loyal to them gains competitive advantage. The commission given to agents or brokers is important because insurance companies who give high commission or treat their agents/ brokers in a special way are considered better. Insurance companies are also using location and hours of business to gain competitive advantage. Some companies have established branch offices to acquire business and therefore taking business services to the people (College of Insurance, 2000).

The insurance premium finance business is still in its infancy in Kenya, having started in 1996. Industry sources indicate that the current players in the market currently finance only 20% of the insurance premiums paid every year in Kenya. Some of the other players in the insurance premium finance market are commercial banks and Triple A Capital Ltd. AAR Credit Services Ltd is well positioned to accumulate significant market share in the industry because of the following main reasons: -

i. Major investment in back-office computer systems that significantly reduces operational exposures;
ii. Superior human resource pool backed by years of relevant experience; and
iii. Solid strategic partnership with highly skilled and well entrenched market leaders in investment banking, pre-paid health management and banking and lending services.

The service environment has evolved due to the following factors: changing patterns of government regulation, technological innovations, the service quality movement, pressures to improve productivity, relaxation of previous professional association restrictions on marketing, internationalization and globalization, e.t.c. (Lovelock et al, 1996). This has caused a lot of dynamism in the service sector: competition has increased and consumers are exposed to more information.

The services industry is not exempt from these environmental changes and suffers from stiff competition within the industry and from price sensitive clients. In some instances service providers extend credit terms to their clients at no extra cost; this adversely affects financial service companies as their services are not required for short term funding. To survive, service companies have to differentiate themselves mainly by being as close to the customer as possible. This has led to an overemphasis in the area of service marketing to enable marketers in developing service strategies to respond to the market (Kimonye, 1998).

1.1.3 AAR CREDIT SERVICES LIMITED

AAR Credit Services was established in May 1999 primarily to improve the renewal rate of AAR Health Services members in addition to growing the membership portfolio by removing the large one-time cash flow requirement of new subscribers. It was registered as a division of AAR Health Services Ltd. In 1997, AAR Health Services Ltd commissioned an independent market research organisation to conduct a survey to determine the main cause of the low renewal rate of individual AAR members. At that time, only 65% of individual AAR members renewed their membership every year. The survey established that for many members, paying membership fees annually in advance was onerous. This was particularly so when paying for a whole family. At that time, other premium finance organisations were providing membership financing services to AAR members but many were not comfortable with dealing with a third party.

At the time of AAR Credit Services' establishment, other premium financing companies were advancing an average of Kshs 2 million per month to AAR members. Upon registration, AAR Credit Services embarked on an aggressive growth strategy with a very limited marketing budget and by the third month was already lending Kshs 5 million per month. Today AAR Credit Services lends in excess of Kshs 20 million per month. In May 2000, AAR Credit Services was registered as a separate limited liability company and in May 2003 it opened its first subsidiary, AAR Credit Services Tanzania Ltd. Its second subsidiary, AAR Credit Services Uganda Ltd was opened in May 2004.

In Kenya, AAR Credit Services Ltd has an employee base of 6 employees. It uses the AAR marketing network of 300 agents and insurance brokers to sell its products. The agents and insurance brokers are paid a commission by the insurance company or HMO for all the premiums financed through AAR Credit Services. The agents and brokers are paid the full commission for premiums financed in much the same way as they are paid for premiums that do not require financing. The organisation structure of AAR Credit Services Ltd is made up of the Board of directors, the chief operating officer, the finance

& administration manager, an accountant for Kenya, a regional accountant for the Uganda and Tanzania office, the customer service executive and the assistant accountant.

The core business of AAR Credit Services is the financing of health membership subscriptions and insurance premiums. Currently, AAR Credit Services has contracted with AAR Health Services and a number of insurance underwriters to finance customers who wish to pay their annual premiums and health subscriptions in monthly instalments. Similarly the Company also finances the payment of annual subscriptions for Wananchi Online Internet/e-mail services. Included in these contracts is an undertaking by the respective service providers to refund AAR Credit Services the pro-rata unutilised portion of the borrower's annual premium/subscription in the event of their default in payment.

In the loan agreement between the borrower and AAR Credit Services, the borrower gives their consent to have their insurance policy/membership service cancelled 7 days after default of any payment. The borrower is also required to pay in advance the equivalent of 2 or 3 months' premium/subscription at the time of receiving the loan. Thus when default occurs AAR Credit's recourse is only to the underwriter for the refund of the pro-rata unutilised portion of the premium/subscription.

AAR Credit Services has also entered into the consumer loan business, where it finances short term loans to staff and agents/brokers of AAR Health Services. Repayments for these loans are through payroll check-off or commission deduction. The Company's state-of-the-art IT system caters for a wide variety of loan products, and has ample capacity for handling a large volume of consumer loans (AAR Credit Services Ltd, Company Profile, 2005).

1.2 STATEMENT OF THE PROBLEM

All organisations are environment dependent. There are enough stakeholders in the environment to jeopardise the chances of success for any given organisation. A fundamental change in the business environment is likely to create pressure for change in an organisation. Any specific factor in the business environment will affect some organisations more than others. Also, it will affect some organisations favourably whilst posing a threat to others. It is imperative for organisations to continuously study the environment and respond to its dynamism, heterogeneity, instability and uncertainty if they are to retain their competitive advantage.

Changes have taken place affecting Kenya's business environment. We would expect organisations to have responded to these changes. Several studies have been done on these changes and they include; Njau (2000), Kandie (2001), Thiga (2002), Kiptugen (2003) and Mutua (2004). AAR Credit Services Ltd is a financial services company that does not fall under the banking Act. None of the studies carried out on responses to environmental changes show the uniqueness of a non-bank financial services company, like AAR Credit Services. AAR Credit Services Ltd is an organisation operating in Kenya. It provides unique financial services in a turbulent industry. It would be expected to respond to the environmental changes as well. Currently it is not known if it has responded to these changes. We would also expect AAR Credit Services Ltd to have responded to these changes as well. Has it responded to these changes affecting the business environment?

1.3 OBJECTIVE OF THE STUDY

This study addresses one objective. This is to establish responses by AAR Credit Services to changes in the environment.

1.4 IMPORTANCE OF THE STUDY.

The results of this study may be of benefit to various stakeholders.

Firstly to shareholders and management in formulating polices that will ensure the continued existence of AAR Credit Services in the long run.

Secondly to other organisations that may face similar environmental changes.

And lastly for academia and research purposes as the findings will add to the existing body of knowledge in areas of business finance and also provide a base for further study in the areas identified.

CHAPTER TWO: LITERATURE REVIEW

2.1 CONCEPT OF STRATEGY

'Strategy is the direction and scope of an organisation over the long term, which achieves advantage for the organisation through its configuration of resources within changing environment and to fulfil stakeholder expectations' (Johnson and Scholes, 2003: 10). Strategy provides management with a future orientated framework for understanding how external forces impact an organisation's performance. Strategy is about creating a fit between the external characteristics and internal conditions to solve a strategic problem. The strategic problem is a mismatch between the internal characteristics of an organisation and its external environment. Firms are in trouble if they do not work on their future (Aosa, 1998).

Further, according to Johnson and Scholes (2003), there are three levels of strategy: corporate, business and operational. Corporate level strategy is concerned with the overall purpose and scope of an organisation and how value will be added to the different parts (business units) of the organisation. Business level strategy on the other hand is about how to compete successfully in particular markets. The concerns are on how advantage over competitors can be achieved; what new opportunities can be identified or created in markets. Operational level strategy is concerned with how the component parts of an organisation deliver effectively the corporate and business level strategies in terms of resources, processes and people.

According to Flavel and Williams, (1996), a business enterprise will justify its existence, and survive in the long term by ensuring that their strategies contain goals, policies, and action sequences. The strategies should be developed around a few key concepts that deal with the unpredictable and the unknown in the environment. This involves various strategy dimensions which include identification of a market need, either latent or currently existing as well as creation of customers and thus, demand for the identical product or service, within sustainable market niche of sufficient magnitude to provide an adequate return to the business.

The strategies also require fulfilling the identified need to the complete satisfaction of its customers, monitoring and anticipating changes to the customers' needs and wants. Monitoring and anticipating competitors' strategies and actions. It calls for monitoring and anticipating changes with the market environment and also formulating strategies, and implementing and evaluating actions, to maintain an on going relevance of the enterprise to its identified market. Strategic planning enables the achievement of these important survival factors in a disciplined, structured and co-ordinated manner.

2.2 STRATEGIC MANAGEMENT

Strategic management includes understanding the strategic position, strategic choices for the future and turning strategy into action (Johnson and Scholes, 2003). Strategic position is concerned with the impact on strategy of the external environment, internal resources and competencies, and the expectations and influence of stakeholders (Johnson and Scholes, 2003). Strategic choices involve understanding the underlying bases for future strategy at both the corporate and business unit levels and the options for developing strategy in terms of both the directions and methods of development (Johnson and Scholes, 2003).

The strategic management process enables an entity to predict its environment and shape its future. It provides information that enables an enterprise to:

i. Avoid consistent short-term focus.
ii. Be more pro-active than reactive. It should never be caught totally by surprise by changing external and market place factors.
iii. Capitalise on its strengths to take advantage of opportunities, and avoid or reduce the impact of threats.
iv. Correct its weakness to take advantage of opportunities, and avoid or reduce the impact of threats.
v. Increase productivity and ensure the long term performance and survival of the business.
vi. Enhance organisation performance and rewards accruing to the stakeholders.

Strategic management is a process with a great deal of promise. However, only in a small number of cases is its full potential realised. Fewer still are the instances of successful adoptions of strategic management. Strategic management has helped organisations to be more proactive than reactive in coping with the changes in their external environment.

Porter (1980) ascertains the value of strategic management to any organisation is to provide a central purpose to the activities of the organisation, the people who work in it (internal environment) and often the world outside (external environment). This can be summarised as the organisation vision, mission and objectives.

Strategic management enables organisations to adjust to the different conditions or pressures due to the changing external environment. Organisations change and often create their environment by focusing on the strategic issues. Porter (1980) goes on to explicitly say that strategic management helps companies develop sustainable competitive advantage. To develop strategy they need to carry out an analysis of the organisations external and internal environment. This enables the organisation to be proactive to the changing environment rather than reactive.

Strategic management helps organisations focus on their competitive efforts, be more effective in resource allocation and identify their key success factors. This ensures that organisations are looking at long term implications of their plans hence creating a culture of a learning organisation. Strategic managers need to understand the concept of strategy as they view their environment in all it perspectives.

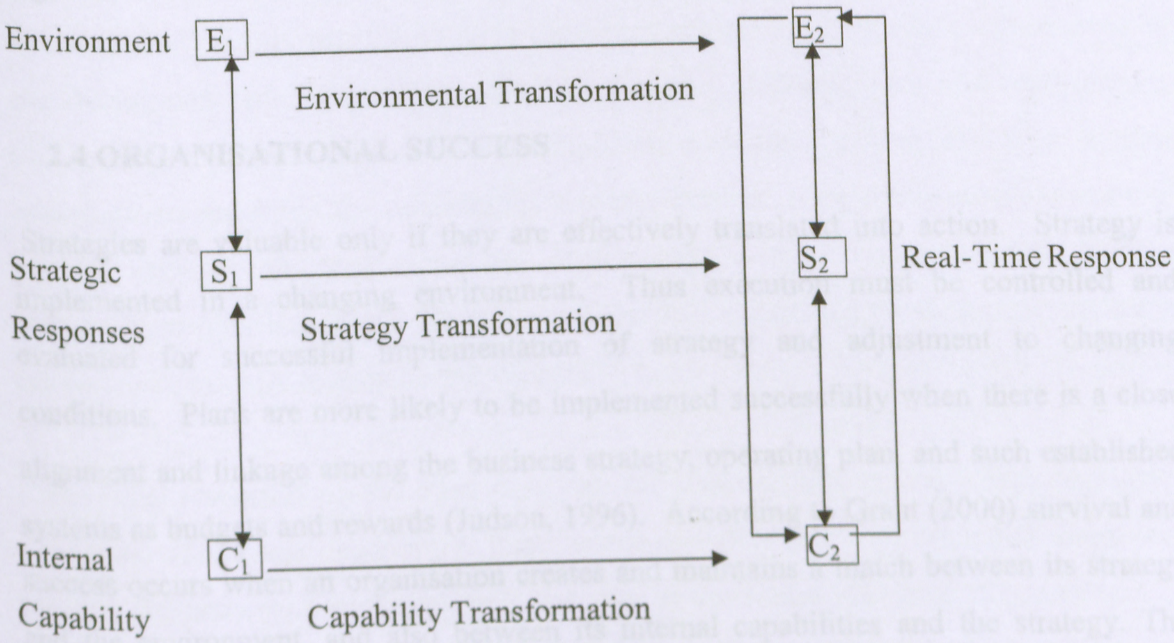
2.3 ORGANISATIONS AND THE ENVIRONMENT

Organisations exist in a complex commercial, economic, political, cultural and social environment. This environment is not static but is under constant change which invariably affects the organisations that operate within it. These environmental changes are more complex to some organisations than others. For survival, an organisation must maintain a strategic fit with the environment. The environment is important and an organisation has to respond to its dynamism, heterogeneity, instability and uncertainty (Thompson 1967). In addition, the competitive environment has been and continues to be driven by technological innovation, globalisation, competition, and extreme emphasis on price, quality and customer satisfaction. As a result, organisations must continuously create and innovate in order to stay relevant and be successful. A sustainable competitive advantage is achieved when there is a strategic fit between the external and internal environment. An organisation's external environment includes economic factors, social, cultural, demographic and technical factors while its internal environment includes organic systems, policies, resource capability and corporate culture (Pearce and Robinson, 1997).

Sauve (2002), noted that, the environment is a critical factor for any organisation's survival and success. It should be seen as a biosphere in which individuals and organisations live over the long term and as a community project in which to be actively involved. It is a resource to be managed and to be shared, hence the need to effectively manage the value chain system, establish collaborations, partnerships and to get involved in social responsibility. This will enrich this resource and enhance the corporate image of the organisation. It is noted that many organisations are now more than ever being involved in social responsibility activities since a good corporate image can also be a source of competitive advantage (Pricewaterhouse Coopers, 2001).

Ansoff & McDonnell (1990) stated that the changes in the organisation's behaviour are necessary to ensure success in the transformation of the future environment. They noted that such changes, which touch on organisation's strategy and capability, need to be systematically identified through the strategic diagnosis approach. This approach is derived from the strategic success hypothesis, which states that a firm's performance potential is optimum when the aggressiveness of the firm's strategic behaviour matches the turbulence of its environment; the responsiveness of the firm's capability matches the turbulence of its strategy; and the components of the firm's capability are supportive of one another. When any of these three aspects are lacking then the firm's performance potential will be less than optimum. The real-time response is to specific action that is chosen and implemented in order to realign the organisation's strategic aggressiveness to the environmental turbulence.

Figure 1: Managing the Firm's Adaptation to the Environment.



Source: Ansoff & McDonnell, 1990, pp 40

Figure 1 clearly indicates the environmental dependence of an organisation. When there is an environmental shift from E_1 to E_2, then the organisation's strategy has to be changed from S_1 to S_2 in order to adapt to the changed environmental conditions. However, this is only possible when organisation's capability is changed from C_1 to C_2. Thereafter an organisation has to monitor its environment continuously so that it can identify any shifts that require it to adjust its strategies in response to such changes. This requires that a firm's capabilities be constantly updated to ensure that they support the chosen strategy.

As the organisation's environment changes it is necessary that the firm continuously adapts its activities and internal configurations to reflect the new external situation. Failure to do this endangers the future success of the organisation (Aosa, 1998).

Porter (1985) explains the concept of dynamic strategic fit. He states that firm's create and sustain competitive advantage because of the capacity to continuously improve, innovate and upgrade their competitive advantage over time. Upgrading is the process of shifting advantage throughout the value chain to more sophisticated types and employing higher level of skill and technology.

2.4 ORGANISATIONAL SUCCESS

Strategies are valuable only if they are effectively translated into action. Strategy is implemented in a changing environment. Thus execution must be controlled and evaluated for successful implementation of strategy and adjustment to changing conditions. Plans are more likely to be implemented successfully when there is a close alignment and linkage among the business strategy, operating plan, and such established systems as budgets and rewards (Judson, 1996). According to Grant (2000) survival and success occurs when an organisation creates and maintains a match between its strategy and the environment, and also between its internal capabilities and the strategy. The environment is not static but turbulent, discontinuous and uncertain.

Strategic responses call for organisations to change their strategy to match the environment and also to transform or re-design their internal capability to match this strategy. It involves identifying changes taking place in the environment and establishing how they affect the organisation and its activities. It also entails determining resources and competences of the organisation and ascertaining whether these provide special advantages or yield new opportunities. Strategic responses result in restructuring the organisation and adopting changes in information technology, changes in the marketing of products or services and culture changes.

This requires that an organisation's internal resources, which include both the tangible and intangible resources, maintain a strategy fit in its values chain system. Failure to match an organisation's structure to the environment will create a strategy gap, while an organisation that fails to match the internal capability to strategy will experience a capability gap. Njau (2000) in his study on the East African Breweries Ltd noted that a change in the company position requires organisations to decide on the strategy to adopt. Bett (1995) established that due to the economic reforms in Kenya, firms in the dairy industry made substantial adjustments in their strategic marketing variables.

Kombo (1997) also noted that firms in the motor vehicle industry made adjustments by introducing new technologies in product development, differentiation and segmentation and by targeting their customers with improved customer services. All these studies among others emphasis the relationship between external competitive environment and internal organisations operations. As is the case with all organisations, Kenyan organisations must recognise the importance of this relationship and nurture the same continuously in order to survive and succeed.

Operational responses on the other hand call for organisations to make decisions under conditions of risk and uncertainty. These decisions reflect the environmental forces that those individuals cannot control, but that may in the future influence the outcomes of their decisions. Each organization is a collection of unique resources and capabilities that provides the basis for its strategy and the primary source of its returns. In the 21st-century hyper-competitive landscape, a firm is a collection of evolving capabilities that is managed dynamically in pursuit of above-average returns. Thus, differences in firm's performances across time are driven primarily by their unique resources and capabilities rather than by an industry's structural characteristics (Ansoff & McDonnell, 1990).

An organisation that has been able to create and maintain consistency or a match between its strategy and environment and a match between its internal capabilities and strategy has greater chances of survival and success (Ansoff & McDonnell, 1990).

The business environment in Kenya drastically changed during the 1990's and the most visible of these changes has been economic reforms, which led to liberalisation and privatisation of state owned companies. This and other changes have created challenges to all organisations irrespective of whether they are for profit or non-profit. In a study of strategic responses by Telkom (K) Ltd undertaken by Kandie (2001) it was noted that there was a need by public companies to come up and implement strategies that aim at making the companies competitive in the market. Studies on responses on the environment have identified some of the responses as: organisational culture changes, operational changes, marketing strategies, technological innovations, improvement in service quality and e.t.c.

Organisations are dependent on their environment. Where there is a shift in the environment this requires a shift in organisation strategy, likewise the internal capabilities. This will enable it support the new strategy responses effectively (Ansoff McDonnell, 1990). An organisation's competitive advantage may thus reside as much in the environment as in the individual organisation. The challenge to organisations is to continuously change their strategy to match the environment and then transform internal capabilities in order to survive, succeed and to remain relevant (Porter, 1985).

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 RESEARCH DESIGN

This is a case study aimed at establishing the responses by AAR Credit Services to changes in environmental conditions. It was an in depth exposition of the changes that have taken place in the six years since its inception that have had a bearing on AAR Credit Services Ltd and how the company has responded to the changes. The research design adopted was geared towards collecting as much data as possible, in order to ascertain whether AAR Credit has responded to changes in environmental conditions as there is no documentation available on the same.

3.2 DATA COLLECTION

Data was collected by way of conducting personal interviews with the five staff of AAR Credit Services. The staff comprised of the managing director, the finance and administration manager, the accountant for the Kenyan operations, the customer services executive and the regional accountant. An interview guide was used to facilitate the data collection processes. The interview guide had open-ended questions. The data was collected in October 2005 and the exercise took three weeks mostly due to availability on the part of staff being interviewed. Some of the staff members interviewed have been in employment with AAR Credit Services since its inception. They have therefore been instrumental to the changes adopted by the company over the years. The interview sought to establish how AAR Credit Services has responded to the changing environment that it operates in.

3.3 DATA ANALYSIS

In-depth data was collected in this research. The in-depth data was analysed using content analysis. Content analysis is a systematic, detailed description of the objectives of the study. This method enabled the researcher to analyse and logically group the data and compile the results of the study.

CHAPTER FOUR: DATA ANALYSIS AND FINDINGS

4.1 ENVIRONMENTAL CHANGES AND RESPONSES

Several changes have taken place in the business environment over the last six years since inception of AAR Credit Services Ltd. Some of these changes have had a bearing on the operations of AAR Credit Services Ltd.

4.1.1 INCREASE IN COMPETITION

The premium finance market has become very competitive with new entrants like commercial banks offering premium financing at interest rates that are lower than the cost of funding sourced by non- banking institutions like AAR Credit Services. Commercial banks have embarked on aggressive marketing campaigns to draw customers for their insurance premium financing product. As a result, customers for this product are more enlightened and have bargaining power on the interest rates to be charged for insurance premium financing. This change in the environment posed a threat to AAR Credit Services forcing AAR Credit Services to re-think its marketing strategy if it was to remain competitive in this market.

To overcome this threat, AAR Credit Services identified and entered into partnership with one of the top insurance companies, namely American Life Insurance Company Limited (ALICO) in 2001 to offer certain value added products to the existing AAR customers. These products proved to be very successful and resulted in an increase in insurance premiums for ALICO by Kshs 19 million in the first year of this initiative. This figure grew to Kshs 30 million in the second year but in the third year the amounts decreased drastically to stand at Kshs 14 million. This reduction was as a result of regularisation of premium rates to be charged by the insurance companies by the Association of Kenya Insurers (AKI). The regularisation of the rates charged for premiums removed the competitive edge that some insurance companies had over their competitions.

Based on the strength of this experience with ALICO, AAR Credit Services continued to enter into strategic partnerships with other Blue chip companies. In 2002 AAR Credit

Services in partnership with Caltex Oil (K) Limited, designed a prepaid fuel card targeting AAR members only. Under this arrangement AAR members are entitled to Kshs 2/- as a discount for every litre of fuel consumed. However unlike the ALICO initiative this product did not generate the expected number of clients and only achieved a client base of 200 clients from the expected 1,500 clients in a period of one year. This was due to technological challenges at Caltex as far as obtaining authorisation for the available amounts for clients to draw fuel were concerned. With time people lost confidence in the product and discontinued its use leaving only a handful of individuals using the product today. The product is still viable and is being re-visited following the general increase in fuel costs.

Other partnerships entered into include cross marketing of products between AAR and Barclaycard. This entailed allowing Barclaycard to target the AAR customer base for the Barclays MasterCard and Visa Card, while AAR Credit in partnership with ALICO targeted the Barclaycard holders with a one million Personal Accident cover. The Personal Accident cover was run for a period of one year and it generated a premium of Kshs 1.8 million for ALICO and a finder's fee for AAR Credit Services. AAR Credit Services also entered into an arrangement with Wananchi Online in 2003, one of the fastest growing Internet Service Providers in Kenya, to finance the payment of their annual internet subscriptions on a monthly basis.

In July 2003, AAR Credit Services was appointed as a Post Paid dealer for Safaricom Ltd, the leading mobile phone operator in Kenya to offer Post Paid Safaricom services to AAR members. A mail shot containing the Safaricom Post paid information was sent to a cross section of AAR members inviting them to subscribe to the Safaricom Post Paid service. A lot of interested was shown for this product but the uptake was not as quick as anticipated as it required active personal selling. Active selling efforts by the sales force engaged to promote this initiative resulted in a client base of 500 in the space of nine months. As the costs incurred by the sales team in terms of their monthly retainer, telephone and travel costs were not sustainable, the sales attained so far were maintained and the sales force discontinued.

Other initiatives undertaken included the design of a medical product targeting the low income group. The brand name for this medical product is 'Afya' and it is an initiative undertaken in 2003 by AAR Credit Services in partnership with AAR Health Services and K-Rep Bank. The initial uptake in terms of the number of people who bought this 'Afya' product was low, with only 200 members drawn only from the K-Rep Bank data base during the year and half period which was a pilot run. The product is now currently offered to AAR corporate members for those wishing to avail a more affordable health benefit to a wide span of employees within the AAR customer base as well. The total number of members who had enrolled on this low income medical scheme as at October 2005 was 3,215.

A special loan product for AAR staff and agents was introduced by AAR Credit Services after a need was identified for this product within the AAR group in 2002. The product has proved to be very popular as most individuals require short term loans payable in about six months that are easily accessible. The loan amounts disbursed are in the region of Kshs 3 million per month. Currently AAR Credit Services is in communication with Afya Sacco which has a membership base of 45,000 Afya members to partner in extending the employee loan product to the Afya Sacco members.

AAR Credit Services has to continually enhance these initiatives as they are copied by the competitors from time to time. The above are all part of AAR Credit Services' diversification plans in a bid to remain competitive in the industry and meet the company objectives.

4.1.2 THE ECONOMY

The Kenyan economy has not performed well over the last couple of years. The effect of the poor economic conditions coupled with the high rate of inflation has led to increased poverty. This has resulted in many corporates retrenching their employees as the businesses are not able to retain all staff with reduced production/sales volumes. At both the corporate and individual level fewer people are able to renew their AAR Health memberships and or insurance covers as their financial status is affected by the economic conditions. This means on the one hand that the actual numbers insured from one period to the next are less, however on the other hand more people now require financing to pay the insurance premiums and / or membership fees monthly as opposed to paying annually in advance. This is additional business for both commercial banks and non-bank institutions like AAR Credit Services offering monthly financing options, as individuals will now seek to borrow to pay for their health and other insurance policies. As a result of the above the volumes of business financed by AAR Credit Services has continued to increase over the years as can be seen from table 1 below.

Table 1: Membership Amounts Financed by AAR Credit Services Ltd in the Last Six Years

Year	Amount in Kenya Shillings (Millions)
2000	70
2001	140
2002	251
2003	220
2004	300
2005	310

Source: AAR Credit Services Internal Records

It is worth noting that the poor economic conditions also adversely affect the purchase of other products and services like assets and the purchasers of these items now require monthly financing options. This creates an opportunity for financial organisations to widen their product range by developing products geared towards financing assets and extending loans to those interested in making purchases of this kind.

To take advantage of this opportunity, AAR Credit Services developed an asset financing product in 2005. It has agreements with organisations like The Copy Cat Limited and Sharp Electronics Limited to offer a monthly payment mode for their products through AAR Credit Services.

4.1.3 SOURCES OF FUNDS

The good track record by AAR Credit Services with its various financiers, namely commercial banks that wholesale funds to the company has continued to attract different banks who want to work with AAR Credit Services Ltd. This has given AAR Credit Services an edge enabling it to negotiate the cost of funds borrowed for onward lending to its customers on a monthly basis. Some of the financiers of AAR Credit Services Ltd have also undergone changes that have an impact on AAR Credit Services. For example First American Bank Limited one of the financiers of AAR Credit Services was taken over by Commercial Bank of Africa Limited (CBA) in early 2005. Prior to this takeover AAR Credit Services benefited from the swift decision making policy and lack of bureaucracy from First American Bank Limited as is the case with small banks.

One of the demerits of the takeover is the slow decision making process and bureaucracy from CBA, which is common to large organisations. As a result of the slow decision making process AAR Credit Services is not able to respond swiftly to take advantage of business opportunities that it encounters from time to time. This necessitated AAR Credit Services to seek for additional alternative funding sources to mitigate this factor. It therefore sought and obtained funding from Equity Bank Ltd in June 2005. The takeover by CBA has its merits from which AAR Credit Services benefits and they include having a large pool of funds now available for lending as the asset base of Commercial Bank of Africa Limited is much larger than that of First American Bank Limited.

The conversion of Equity Building Society to Equity Bank Ltd availed another source of funds for AAR Credit Services Ltd. Equity Bank is another of the banks that AAR Credit Services has an agreement with for wholesale of funds for on-lending to customers for premium financing as well as financing of its other product lines.

4.1.4 CHANGE IN THE AAR HEALTH SERVICES PAYMENT POLICY

The insurance premiums and health membership fees in most countries in Europe, United States of America and South Africa are actually paid on a monthly basis as opposed to an advance single annual payment. AAR Health Services Ltd changed its policy on payment of the health membership fees from a single annual payment which is quite onerous to a more affordably monthly payment plan policy in 2005. For the vast majority of people income is earned on a monthly basis, it is therefore envisaged that this transition from the annual payment mode to the payment of the AAR membership fees in monthly instalments, will make the product more attractive and affordable to a wide spectrum of people. AAR is a household name and the dominant Health Maintenance Organisation in the East African region. This goodwill has had a very positive impact for AAR Credit Services Ltd. This transition by AAR Health Services will be managed by AAR Credit Services Ltd and will result in an increase in the business financed by AAR Credit Services on a monthly basis.

The collapse of some of the Health Maintenance Organizations (HMOs) in Kenya has also been a challenge to AAR Health Services as clients are reluctant to buy products offered by HMOs because they are not sure of their future in the Kenyan business environment. An aspect of this challenge has been positive for AAR Credit Services as some clients now opt to pay the monthly AAR Health membership through AAR Credit Services as opposed to paying the fees annually in advance.

4.1.5 DEVELOPMENTS IN INFORMATION TECHNOLOGY

Information technology has continued to evolve over the years and more advanced methods of capturing and availing information are now in use making operations more efficient. AAR Credit Services has continually benefited from these changes in technology and boasts of a small staff of 6 (six) to date even though it has increased the amounts financed at least ten-fold since its inception six years ago. The banking industry has also embraced the new technology and most of the banks that AAR Credit Services Ltd works with for financing now have internet banking facilities available. This facility makes it easy for AAR Credit Services to verify its transactions on a daily basis at its own convenience without relying on bank personnel.

Innovations in technology have also made it possible to create interfaces between systems in use by AAR Credit Services. At inception in 1999 AAR Credit Services used simple spreadsheets to capture the various loans for amounts advanced to finance its different products. These records were to a very large extent maintained manually. In the year 2000 an elaborate software program, Insurance Premium Finance (IPF) was tailor-made to suit the various products offered by AAR Credit Services. The IPF program enabled the maintenance of the individual loan accounts as well as the production of various management information reports. In addition the IPF program has a calendar that enables the tracking of mature loans on a daily basis. It also provides an archive system that makes statistics available for decision making by management.

For the finance and accounting of the company's operations the Solomon IV accounting program was purchased in 2001. This accounting program replaced the manual spreadsheets previously used for purposes of accounting and financial reporting. However at that time the IPF program used for maintaining the loans and the accounting program were not linked resulting in a lot of duplication of transactions as they had to be posted into both programs. In 2003 the two systems were linked by creating an interface which allows for transactions to be exported from the IPF program to the Solomon IV accounting program. This interface has had the positive impact of enabling AAR Credit Services to increase its product offering as well as the level of business without necessarily increasing the number of human resources.

The IPF program is under constant development and enhancement to cater for the changing product requirements by AAR Credit Services. Some of the enhancements include automation of the receipt process from issuing manually written receipts to computer generated receipt copies. Other enhancements include the generation of management reports and statistics on the loans issued from the IPF program to replace the manual reports produced previously. A number of data capture screens have also been modified over the years to facilitate capture of additional information in the IPF program to meet the requirements by management. Innovations in technology have also helped to reduce duplication of tasks and also eliminated redundant tasks that are common in manual or partly automated processes.

4.1.6 AAR CREDIT MANAGEMENT TEAM

Initially AAR Credit Services had a team made up of the managing director and a secretary on a full time basis and the services of the chief accountant of AAR Health Services on a part time basis for finance and operations related issues. AAR Credit Services originally financed the AAR Health membership fees only. Over the years the product range has increased and the amounts financed have risen as stated earlier. In response to this change the management team has been strengthened and is now made up of the managing director, the finance and administration manager, three chartered accountants and a customer service executive. It is small enough to facilitate swift decision making and quick implementation of changes that are required from time to time.

Some of the key areas that the team concentrates on include the simplification of documentation to be used for application of the AAR Credit Services loans and ensuring that the turn-around time for processing all applications received, is within reasonable limits for each of the range of products currently available. AAR Credit Services also promotes learning and training in different areas for its staff. It ensures that the different personnel are empowered to make decisions in their respective work areas as the procedures are clearly defined and are reviewed often.

As part of its plans to remain profitable and competitive in the market AAR Credit Services now organises sessions to discuss the strategy that the company should adopt continually with the Board of Directors and the Management team. This helps AAR Credit Services to focus on its competitive efforts, be more effective in resource allocation and identify the key success factors. This ensures that the organisation looks at long term implications of its plans hence creating a culture of a learning organisation.

The responses above by AAR Credit Services may have served well in the past but they are not adequate to ensure its competitiveness in the long run as the environment it operates in is not static. Most of the responses mentioned above will not necessarily guarantee a competitive edge for the organisation in the future as some of the responses are easily copied by the competition with time. Therefore AAR Credit Services must actively identify the needs of its current and potential customers and continuously create and innovate in order to stay relevant and be successful.

CHAPTER FIVE: SUMMARY AND CONCLUSION

5.1 ENVIRONMENTAL CHANGES

The business environment within which AAR Credit Services Ltd operates continues to change dramatically posing challenges to its operations. From the findings it has become apparent that AAR Credit Services Ltd has been affected by the changes in the external environment. These include increase in competition especially from commercial banks, a poor economic environment, and advancement in information technology. These changes mean that AAR Credit Services Ltd has had to respond in order to maintain its position and possibly increase its market share.

5.2 RESPONSES TO CHANGES

The study established that AAR Credit Services Ltd has responded to these changes and challenges by coming up with several measures. These measures include identifying and entering into strategic partnerships with both service providers (like AAR Health Services, Safaricom, AIG, Caltex, e.t.c.) and commercial banks (like Commercial Bank of Africa, K-Rep Bank and Equity Bank). It has also diversified and offers a wide range of affordable products as well as promoting a learning culture within the organisation. AAR Credit keeps abreast with technology by enhancing the IT systems to create efficiencies in the processes. Other responses comprise actively involving the directors and the management team in strategy sessions, aimed at obtaining a better understanding of the changing environment of this millennium through enlightened diagnosis of the potential threats and opportunities that it poses for the organisation.

5.3 LIMITATION OF THE STUDY.

There were some limitations encountered during this study. Firstly is the fact that generalization is not possible and therefore the findings may not apply to other financial services companies, Secondly the study also relied mostly on the information gathered during the interview as very little documentation is available from the organisation under study. Another limitation of the study is the lack of secondary data in the initial stages of designing the interview guide, this was due to the limited information available in the public domain. .

5.4 RECOMMENDATION FOR FURTHER RESEARCH

Currently AAR Credit Services specialises in niche marketing for all its product lines. Given that the environment is not static, it is recommended that studies be undertaken to identify areas that AAR Credit Services has competencies to enable it achieve the coveted competitive advantage in the industry it operates in.

It is also recommended that studies can also be undertaken to establish the needs of the AAR customers to facilitate the introduction of other value add products that will complement the existing capabilities and also identify a gap in capabilities that AAR Credit Services must acquire for the new products to be launched.

A further recommendation is that similar studies be conducted to establish how the other institutions in Kenya are responding to the environmental changes.

APPENDIX 1

LETTER OF INTRODUCTION

October 2005

AAR Credit Services Ltd
Williamson House
P.O. Box 41766 00100
NAIROBI

Dear Sir/ Madam,

I am a post graduate student in the School of Business, University of Nairobi. I am conducting a management research on the responses by AAR Credit Services Ltd to changes in the environment.

In order to undertake the research you have been selected to form part of the study. This letter is therefore to request your assistance in collecting information to enable me carry out the research. The information you give will be treated with strict confidentiality and is needed purely for academic purposes; even where a name has been provided, it will not under any circumstance appear in the final report.

A copy of the final report will be available to you upon request.
Your assistance and co-operation will be highly appreciated.

Yours sincerely

Margaret Njoroge
Student

Professor E. Aosa
Lecturer Department of Business
Administration (Supervisor)

APPENDIX 2

INTERVIEW GUIDE

Part A ENVIRONMENTAL CHANGES.

1. What external changes have taken place that may have affected the operations of AAR Credit Services?
2. Indicate how the changes may have affected AAR Credit Services.
3. What challenges (if any) do these changes pose to AAR Credit Services?

Part B RESPONSES TO ENVIRONMENTAL CHANGES

4. How has AAR Credit Services responded to environmental changes?
5. What are the key performance indicators of the response to change in AAR Credit Services?
6. What measures has AAR Credit Services taken to ensure continued positive trends due to responses taken towards challenges?
7. What would you recommend towards future plans of the company regarding the methodology of responding to the challenges?
8. What would AAR Credit Services do differently now that it overlooked previously?
9. Comment on the ability of the company to respond to relevant external changes?

Thank you very much for your time and co-operation.

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