STRATEGIES USED BY COMMERCIAL BANKS IN KENYA TO MANAGE OPERATIONAL COSTS

BY

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A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENT FOR THE AWARD OF THE AWARD OF THE DEGREE IN MASTER OF BUSINESS ADMINISTRATION (MBA), SCHOOL OF BUSINESS

UNIVERSITY OF NAIROBI

NOVEMBER : 2012

DECLARATION

This is to declare that this research project is my original work that has not been presented to any other University or Institution of Higher Learning for examination.

Signed: ________________ Date: 9th NOVEMBER, 2012.

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This is to declare that this project has been submitted for examination with my approval as the university supervisor

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ACKNOWLEDGEMENT

The completion of this project was not easy. It was not created by the author alone, but relied on the cooperative assistance of many unseen hands. First and foremost I owe special thanks to God Almighty for seeing me through. I sincerely acknowledge my supervisor Dr V. Machuki, Lecturer University of Nairobi, School of Business for his enabling support and guidance.

I would also like to acknowledge the encouragement from all my colleagues and MBA classmates, friends and relatives whose remarkable devotion and dedication throughout the project work was incredible. May God bless the work of their hands!

DEDICATION

This research study is dedicated to my parents Mr. Joseph Paul Obiga and Mrs. Rose Akinyi Obiga, Joseph O. Olando my loving husband and my sons, Kyle and Trevor you really helped me achieve my goals. God bless you all.

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ABSTRACT

Commercial banks like any other institution require sustainability. Any organization over time needs to sustain itself through cost management. The objective of this study was to determine the strategies that are used by commercial banks in Kenya to manage operational costs. The study used cross sectional descriptive survey design in collecting data from the respondents. The target population consisted of all the 43 commercial banks operating in Kenya. Questionnaire was the data instrument used in collecting the primary data. The questionnaire comprised of open ended and closed ended questions which allowed for the collection of as much details as possible. After the collection of data, it was thoroughly examined and checked for completeness and inconsistencies. The data was then summarized, coded and tabulated then analysed using quantitative techniques. In the findings of the study established that commercial banks need to recognize the various cost drivers that affect their operations. The study concluded and recommended that commercial banks need to adopt a number of strategies to manage costs which include mergers and acquisitions, restructuring, business process re-engineering, consolidation of business functions, rationalization of staff fringe benefits, marketing reduction, outsourcing, customer re-organization and technological upgrade.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Business priorities have shifted from growth and leveraging up profits to issues of survival and preserving core assets and competencies. There is an understandable emphasis on cost cutting which is seen as the best way to maintain profits in the face of softening sales and shrinking margins. An organization earns profit when its business costs and expenses are less than its revenue through its services and investment (Blocher, 2009). Any business for that matter survives only if it earns profits. For a company to provide a reasonable return for the huge capital expenditure and to remain servicing the economy, profitability is a must. To remain profitable, efficient and effective cost management of its entire operations is the need of the day for any business (Peacock, 2005).

Current market condition and the economic downturn have changed the financial service environment. One result is an increase focus on strong operational effectiveness. Companies are feeling the pressure on their budgets and currently looking for ways to cut costs without undermining their ability to sustain business as usual (Shield and Young, 1999). The widespread focus on growth combined with lack of discipline around operating models, product streamlining, margin control and organizational structures, has led many banks to build up highly disparate and complex operating models. This in turn has led to high cost bases as well as inflexibility and duplicative operations. A more transformational approach to cost cutting is required to unravel this complexity (Blocher, 2009).

Banks largely operated in an extraordinarily benign environment of low interest rates, rising home prices, expanding loan volumes and robust economies. All of which created opportunities to generate substantial organic growth and shareholders' value. Most banks were able to steadily improve their cost-to-income ratio during that period. But today, high energy prices, sluggish economies and the continuing fallout from the credit crunch have put a damper on the banking industry globally. Many financial institutions have posted huge write downs (Schiff and Schiff, 2008). Leading banks realize the importance of taking out costs and investing the savings in strategic programs that will help them gain competitive advantage (Peacock, 2005). Schiffs and schiffs (2008) argues that financial institutions therefore need to take a more strategic approach by viewing cost cutting as part of a broader efficient effort. Balancing short term tactical cost reductions with long term strategic costs initiatives will leave banks much better positioned for future performance.

1.1.1 The Concept of Strategy

Strategy is a pattern of resource allocation that enables an organization to maintain and improve its performance. Thompson and Strickland (2007) define strategy as a management action plan for running the business and conducting its operations. A strategy is the direction and scope of an organization over the long term which achieves advantage for the organization through its configuration of resources within the changing environment, to meet the needs of markets and fulfill stakeholders' expectations (Johnson & Scholes, 2002).

Strategy is the process by which managers, using a time horizon can develop a sustainable competitive advantage. A company can either adopt a low cost or differentiation strategy. The focus on differentiation strategy is to differentiate the product offering to create something that customers can perceive as unique. The primary

focus for low cost strategy is to achieve cost leadership relative to competitors. Cost leadership can be achieved through approaches such as economies of scale production, learning curves effects, tight cost controls and cost minimization areas such as research and development, services, sales forces or advertisement (Porter, 1997).

1.1.2 Operational Costs

Cost management consists of those actions that are taken by managers to reduce costs, some of which are prioritized on the basis of information extracted from the accounting system. Other actions, however, are undertaken without the use of accounting information. They involve process improvement, where an opportunity has been identified to perform processes more effectively and efficiently, and which have obvious cost reduction outcomes (Drury, 2000). Thus, cost management focuses on cost reduction.

The key success factor in cost management is focusing on the right areas and making decisions based on actual facts on cost items. Companies should not blindly try to use all the strategies as there is no "one size fits all" solution. Instead, they should selectively mix and match (Grant, 1996). The strategies that can be adopted by a company to manage costs include employee layoffs, job elimination, organizations structural changes, employees' compensation reduction, employees' benefits reduction, advertisement reduction, process redesign, shared services, outsourcing and customers' reorganization (Hamel and Prahalad, 2003). These strategies can be categorically applied across all business functions or individual departments. These departments include support, marketing, sales and service, operations and procurement.

1.1.3 Commercial Banks in Kenya

Commercial banks in Kenya are regulated by the Central Bank of Kenya Act (Cap 91) and the Banking Act (Cap 488). These Acts are intended primarily to facilitate the development and maintenance of a sound monetary policy. Currently there are forty three (43) commercial banks, fifteen (15) microfinance and forty eight (48) foreign exchange bureaus in key banking (Bank Supervisory Department Annual Report, 2010).

The banks have come together under the Kenya Bankers Association, which serves as a lobby for the banks interests and also addresses issues affecting the members. The industry is dominated by a few banks which are foreign owned and some are locally owned. The Central Bank of Kenya falls under the docked of the ministry of finance, which is responsible for formulating and implementing monetary policy and fostering the liquidity, solvency and proper functioning of the banking industry.

The key issues affecting the banking industry in Kenya includes changes in the regulatory framework where liberalization exists, declining interests margins due to customers pressure leading to mergers and reorganization, increased demand for nontraditional services and more towards emphasis on the customer rather than the product and the introduction of nontraditional players who offer financial services products.

1.2 Research Problem

Management of the operational expenses is becoming common among firms and the companies that initiate them report varying effects ranging from short term gain and long term competition. The decision to manage operational expenses is made for strategic and financial reasons. The expectation is that reduction in costs will lead to

positive impact on the bottom line and will be reflected in improved profitability and productivity (Stacey, 2003).

The banking industry faces an economic environment of continuous and accelerated changes. The decision to manage operational expenses is made for strategic and financial reasons. The expectation is that reduction in costs will lead to positive impact on the bottom line and will be reflected in improved profitability and productivity. The major challenge for the commercial banks is to come up with strategies that will make them more cost efficient.

A number of studies done mostly focused on factors affecting effective cost management in organizations. For instance Kirtan (2010) researched on the factors influencing effective cost management within South Africa's retail banking sector, Janjua (2011) looked into the cost efficiency analysis of manufacturing companies in Pakistan: based on free distribution approach. There is no known study that has focused on managing the escalating operational costs. This study therefore seeks to fill the existing knowledge gap by investigating the drivers of costs for commercial banks and by answering the question how are commercial banks managing their operational costs?

1.3 Objectives of the Study

The objectives of the study will be to:

i. Establish the cost drivers among commercial banks in Kenya.

ii. Determine the strategies adopted by commercial banks in Kenya to manage the operational costs.

1.4 Value of the Study

With the findings of this study, commercial banks will be in a position to determine the effectiveness of the cost cutting strategies they are currently employing and the challenges faced in the implementation of those strategies. The commercial banks will be in a position to understand better on the strategies they can continue adopting to make them more cost efficient and the new strategies they can implement to make them overcome the various cost management challenges within the industry.

The Government will benefit from the information especially ministry of finance and related agencies in formulating policies that will create conducive operating environment within the banking industry. The government through central bank of Kenya is the policy maker of the bank processes and products offered to customers. The research information will help them in ensuring the policies they create do not pose a threat to the banks operation.

Finally scholars and other research students will find the research data useful for reference purposes and identifying areas of further research. This research can help in directing students on other further research which can be conducted within the banking industry.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter presents the review of literature in support of effective cost management, factors which influence cost management and its alignment with strategy. Literature on the existing operational cost drivers and the cost management strategies are presented.

2.2 The Concept of Strategy

Strategy, a word of military origin, refers to a plan of action designed to achieve a particular goal. It is the match between an organization resources and skills and the environment opportunities it wishes to accomplish. Strategy is more though, than laying out the plan long term or short of what we are going to do. Once strategy is determined, second tier or operational decisions can be made in the proper context. By definition, operational decisions are those that pertain to the broad execution of strategy. After operational decisions come tactical decisions, those third-tier decisions made in the heat of battle. Military tactical decisions are made on the ground during battle. Military tactical decisions are made on the ground during battle when, inevitably, things do not go as planned, and officers and soldiers must improvise as they adjust to changing circumstances. Tactical decisions must be aligned or with strategic and operational decisions. Strategy without tactics is the slowest route to victory. Tactics without strategy is the noise before defeat (Johnson and Scholes, 2002).

Strategy guides organizations to superior performance through establishing competitive advantage. It also acts as a vehicle for communication and co-ordination within organizations. Successful strategies include objectives that are simple, consistent and

long term, good understanding of the competitive environment and objective understanding of resources that is, understanding strengths and exploiting them and understanding weaknesses and protecting the organization against them. Understanding the strategic position of an organization and considering the strategic choices upon to it is of little value unless the managers or management wish to follow can be turned into organizational action (Johnson and Scholes, 2002).

Mintzberg (1990) distinguishes between intended, realized and emergent strategy. Intended strategy is strategy as covered by management. Emergent strategy is strategy that becomes apparent through passage of time, that is, after the events it governs. Realized strategy is the strategy that is observed. It is influenced by both intended and emergent strategy. Strategic management on the other hand is the set of decisions and actions that results in the formulation and implementation of plans to achieve a company's objectives. Organizations whether profit or non-profit making, private or public have found it necessary in the recent years to engage in strategic management in order to achieve corporate goals. They are required to think strategically as never before, need to translate their insight into effective strategies to cope with their changed circumstances, and lastly to develop rationale necessary to lay ground work for adopting and implementing strategies in this ever-changing environment (Pearce and Robinson, 1997).

2.3 Operational Costs

In production, research, retail, and accounting, a cost is the value of money that has been used up to produce something, and hence is not available for use anymore. In business, the cost may be one of acquisition, in which case the amount of money expended to acquire it is counted as cost (Ansoff and MacDonnel, 1990). In this case, money is the input that is gone in order to acquire the thing. This acquisition cost may be the sum of

the cost of production as incurred by the original producer, and further costs of transaction as incurred by the acquirer over and above the price paid to the producer. Usually, the price also includes a mark-up for profit over the cost of production.

Organizations and managers are most of the times interested in and worried for the costs. The control of the costs of the past, present and future is part of the job of all the managers in a company. In the companies that try to have profits, the control of costs affects directly to them (Grant, 1996). Knowing the costs of the products is essential for decision-making regarding price and mix assignation of products and services.

Operational costs can be defined as the day-to-day expenses incurred in running a business, such as sales and administration, as opposed to production. They can also be referred to as operational expenses (Grant, 1996). Operational costs can be described as the expenses which are related to the operations of a business, or to the operations of a device, component, piece of equipment or a device (Peacock, 2005).

In a commercial enterprise, operational costs can be divided into fixed costs and variable costs. Fixed costs refers to the costs which remain same whether the operations are closed or running at hundred per cent while variable costs may increase depending on whether more production is done, and how it is done (Schiff and Schiff, 2008). Variable costs are therefore the costs which can be managed depending on how their cost drivers are handled.

2.4 Operational Cost Drivers

Cost drivers refer to the measures of activity which have a cause-effect link to the incidence of a cost (Arnold and Turley, 1996). Drury (2000) states that cost drivers is used to describe the terms, events or forces that are significant determinants of the cost

of the activities. Therefore, cost drivers represent those factors whose occurrence creates the costs.

Staff salaries/benefits is a cost item in respect to the how many staff members work on activities identifiable by program. Cost per program varies by time required of staff member to complete a task. The possible cost driver would be hours spent on each program by the staff. The numbers of staff members required to work on a program(s) would also be considered a cost driver (Clarke, 1999).

Organization(s) offer a variety of products that's unique to different clientele. The cost drivers would be the number of product, number of unique processes, time required to work on various products and the specific materials required in the manufacturing process of the products. The amount of specific products whose demand by the customers is high and the number of employees involved in the production of these products can also be considered a cost driver (Kren, 2008).

Information technology hardware and maintenance cost varies with the number of people using information technology equipments and units of equipment requiring service. Information technology software licenses cost will vary with the number of licenses. Cost driver in technology would be the number of equipment required to work on a program and the number of staff who are specialists in field of information technology required to work on the programs (Clarke, 1996).

Offering the highest standards of service is key for any organization and as such quality control has been put in their daily services. This cost will vary with the number of services or/and products offered and how much time required in their provision.

The degree of demand by customers for the quality products or/and services is also a cost driver (Kren, 2008). In this light Quality management approach would be the cost driver.

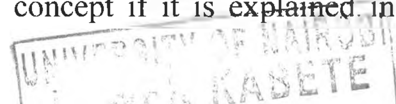
As for shelter, organizations need to put their office in strategic positions ensuring easy access by the public and yet very secure for both the organization and its customers. The cost here will vary with the number of people being housed and space utilised and location of the building. The number of customers visiting a specific branch of the organization and the number of staff members attending to those customers can also be considered as a cost driver. The cost drivers will be the number of office staff and the squire feet occupied by per department (Johnson and Kaplan, 1991).

The number of materials printed, number of advertisements and number of beneficiaries will vary the cost. The possible cost drivers would be materials ordered by product, advertisements produced for each product and number of beneficiaries. The number and nature of audience the advertisement is intended to reach can also be considered as a cost driver (Johnson and Kaplan, 1991).

2.5 Cost Management

Cost management is the process by which companies control and plan the costs of doing business. Businesses should have customized cost management plan, and companies as a whole also integrate cost management into overall business model (Peacock, 2005). When properly implemented, cost management will translate into reduced costs of production for products and services, as well as increased value being delivered to the customer (Blocher, 2009).

For a company's management to be effective overall, cost management must be an integral feature of it. It is easiest to understand this concept if it is explained in the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context of a single project. For instance, before a project is started, the anticipated costs should be identified and measured. These expenses should then be approved before any purchasing occurs. During the process of completing a project, all incurred costs should be noted and kept in a record of same kind, to help ensure that the costs are controlled and kept in line with initial expectations, to the extent that is possible (David, 2002).

Taking this approach to cost management will help a company determine whether they accurately estimated expenses at first, and will help them more closely predict expenses in the future. Any overspending can also be monitored in this way, and either eliminated in future projects or specifically approved if the expense was necessary (David, 2002).Cost management cannot be used in isolation; organizations' operations must be organized and tailored with strategy in mind thus the need for cost management strategy.

If an organization's processes are completely and clearly defined, this facilitates effective management of costs. Effective cost management strategies helps an organization deliver successful results within the allocated budget, while also taking it as valuable as possible to the company. There is always the possibility of unexpected costs, but preparation in the form of cost management will likely make them much easier to deal with when they occur (Blocher, 2009).

2.6 Cost Management Strategies

In an organization, when managers are faced with a cost management decision, the practice usually entails making arbitrary cuts which could result in eliminating value adding activities. However, successful cost management practices are meant to provide a framework to understand and control costs within an organization (Kren, 2008).

The path to high performance starts by understanding the organization's cost anatomy since the organization's cost structure is not spread evenly across the business functions

(Blocher, 2009). The key success factor is focusing on the right areas and making decision based on the specific cost items. Some strategies will apply to all the business functions while others fall in specific business functions (Wheelen and Hunger 2004).

2.6.1 Mergers and Acquisitions

Mergers and acquisitions can be used as an opportunity to both reduce operational costs and achieve an important strategic objective. Mergers refer to any combination of two or more business enterprises into a single enterprise while acquisition is the gaining possession of one enterprise by another (Chamberlain and Sandra, 1998). Joining together of two or more organizations creates opportunities to eliminate overlaps in such areas as back office staff, branch offices and computing infrastructure. The organizations which are joining together can also create a larger and more diversified financial institution which would increasingly have a comparative advantage in attracting new business from corporate and retail customers (Kren, 2008). Mergers and acquisition can therefore also be viewed as a vehicle for increasing top-line revenue growth.

Globalization, technological advances, and regulatory retreat are often cited as factors that have stimulated and allowed more banks to merge. Mergers may reduce costs if they enable banks to close redundant branches or consolidate back-office functions. Mergers may make banks more productive if they increase the range of products that banks can profitably offer. Mergers may also diversify further bank portfolios and thereby reduce the probability of insolvency. Increased diversification then may reduce banks' total costs by reducing desired capital-asset ratios. Increased diversification and size may also raise revenues if they increase banks' attractiveness to customers who will deal only with very safe institutions. Though banks' loan rates or non-interest revenues might rise or their deposit rates or capital requirements might fall as a result of mergers, we do not

focus on those aspects of mergers here. Rather, we focus on the effects of merging on banks' non-interest expenses (Chamberlain and Sandra, 1998).

Mergers and acquisitions are strategic methods to grow business, migrate into other channels of business, and are frequently intended to protect profitability while reducing operating costs. Quite often the approach assumes that revenue will be sustained or enhanced while operational support is simultaneously consolidated and reduced to minimize costs. The intent to protect and boost profit by maintaining revenue and slashing consolidated operational costs is a great theory (Kren, 2008). Mergers and acquisitions are often planned as strategic market expansion during periods of stable economic conditions, and frequently the result of rushed response to slash operational and support costs during the challenging economic periods. Regardless of the catalysts, there are some basic principles to govern the relative success of such a venture. On a large scale, mergers and acquisitions occur when whole organizations combine, collide, or are absorbed. On a smaller scale, departments and groups of individuals within organizations are also being merged, acquired, and absorbed. Big or small, the basic rules for transition remain the same (Hamel and Prahalad, 2003).

2.6.2 Restructuring

Restructuring is the process through which a company radically changes the contractual relationships that exist among its creditors, shareholders, employees, and other stakeholders (Schiff and Schiff, 2008). Restructuring can also be defined as the process of reorganizing where the composition and operations of an organization can be completely changed. Restructuring frequently result in the elimination or replacement of departments and division, causing temporary and permanent layoff (Zack, 1999). The goal of restructuring is to increase the overall market value of the business enterprise.

Restructuring can be either through downsizing or/and retrenchment. Downsizing is the discharge of surplus employees due to down turn in the business. This will result to the reorganization of the employers undertaking; consequently some employees may be redundant and may have to be retrenched. Retrenchment refers to the voluntary action of an organization to reduce expenses (Bruce and Green, 2000). Many scholars have defined retrenchment as a purposeful reduction in the size of an organizations' workforce. Restructuring strategy has been adopted to deal with the economic pressure in an environment. It has been termed as beneficial in terms of economic level, increased operational efficiency and increased productivity (Gandolfi, 2009).

Organizational performance ultimately rests on human behavior and improving performance requires changing behavior. Therefore organizational restructuring should have as a fundamental goal the facilitation of clear, open communication that can enable organizational learning and clarify accountability for results (Zack, 1999). Since the world is continually changing, continuous organizational learning is necessary to stay up to date. Organizations that cannot or will not learn will become obsolete. Leaders should periodically examine the organizational structure of their enterprise to assure that it continues to provide an environment for organizational learning. A non threatening, development focused performance appraisal process can be an effective organizational learning tool.

2.6.3 Business Process Re-engineering

Business process re-engineering refers to the analysis and redesign of workflow within and between enterprises (Barney, 2001). Business Process re-engineering is used for elimination of inconsequential steps, or using less expensive resources for their execution, which is at the heart of noteworthy cost cutting projects.

As initial process design are not always performed with cost efficiency as the highest priority, and since practice moves away from original process design over time, there always exists ways to decrease the cost of operations through economizing process designs. This could simply mean one less approval step in a given process, or the introduction of a complete new way of doing things (Stacey, 2003). Business process re-engineering is also known as business process redesign, business transformation, or business process change management.

Business process re-engineering is basically rethinking and radically redesigning an organization's existing resources (Barney, 2001). Business process re-engineering, however, is more than just business improvision, it is an approach for redesigning the way work is done to better support the organization's mission and reduce operational costs. Business process re-engineering starts with a high-level assessment of the organization's mission, strategic goals and customer needs. Within the framework of the basic assessment of mission and goals, re-engineering focuses on the organizations business processes, steps and procedures that govern how resources are used to create products and services that meet the need of particular customer or markets (Stacey, 2003). Re-engineering identifies, analyzes, an organization's core business processes with the aim of achieving dramatic improvement in critical performance measures, such as operational costs, quality, services and speed.

Business process re-engineering is the analysis and design of workflows and processes within an organization. According to Davenport (1990) a business process is a set of logically related tasks performed to achieve a defined business outcome. Re-engineering is the basis for many recent developments in management. The cross-functional team, for example, has become popular because of the desire to re-engineer separate functional tasks into complete cross-functional processes. Also, many recent management

information systems developments aim to integrate a wide number of business functions. Enterprise resource planning, supply chain management, knowledge management systems, groupware and collaborative systems, Human Resource Management Systems and customer relationship management.

In case of facilities, technology or anything that 'works', companies should hinder from renewals and upgrades, as long as it does not significantly affect operations. This may mean changes in certain organizational policies and configuration of management practices, as most organizations already have periodical renewals and upgrade policies (David, 2002).Most operations not engineered with maximum cost efficiency in mind create some amount of waste of resources and utilities. Eliminating such waste can decrease considerable operating costs, which is why this is one of the most frequently followed guidelines (Barney, 2001).

2.6.4 Consolidation of Business Functions

The consolidation of business activities reduces operational redundancies and eliminates superfluous staff and administrative functions. As a result, operating and capital costs decline, which helps improve the bottom line (Grahame, 2005). A business consolidation leads to the elimination of duplicate assets, which equals financial savings. By reducing the number of facilities in a business, it can save money and operate more efficiently. Consolidation can also improve communication between business functions, such as production and marketing, and achieve savings by decreasing head count and consolidating systems and processes (Grant, 2001).

Replication of activities across branches usually creates utilization inefficiencies in operations. Consolidating certain functions via the utilization of a centralized approach can result in significant savings. For companies operating multi-nationally, it can

become an even bigger cost-cutting initiative (Devine, Ealey and O'clock, 2008). Centralizing all procurement and forgoing what is not in need can also cut on operational costs. For multinational institutions, global procurement centers can tale these savings one step further, leveraging the best deals across nations for products and service needs (Blocher, 2009)

Considering channel close down and relocation is also a strategy in cost management (Grahame, 2005). Companies should look into closure of their unprofitable channels, automated teller machines and branches, in order to decrease cost of sales and services. With decreasing market demand and changing customer needs, certain branches, automated teller machines and channels can become redundant with limited potential, or, expensive to maintain. Relocation is also an alternative to a close down, which can significantly decrease cost of rent and maintenance (Grant, 1996).

2.6.5 Rationalization of Staff Fringe Benefit

Decreasing the cost of human resources can be used as a strategy to manage costs. Financial institutions inevitably need to adjust their compensation policies so as to cost cut. Companies can find ways to decrease costs by focusing on non-monetary benefits or free services which are not vital and would not necessarily create as much dissatisfaction on the employees. Many companies take action to put more restrictions on personal use of corporate services. Although most of these services have negative impact on employees' morale, they are vital in cost management (Devine, Ealey and O'clock, 2008).

Rent and maintenance costs of company buildings may not be considered quite essential during regular times, when compared to the benefit of having more satisfactory work environment and prestigious business address. However, when compared o several alternatives costs cutting measures and the impact of not cutting enough costs, relocation

may become a more preferable option at least for some of the business functions (Grant,1996). In any organization, staff members are usually considered as the company's capital. When taking all aspects into consideration, a company's payroll is definitely the biggest expense and easily becomes problematic. Rationalization measures frequently starts with reducing staff operational costs (Peacock, 2005).

2.6.6 Marketing Reduction

Although traditional mass marketing and advertising activities can be effective ways for increasing overall awareness and interest, they are not the most cost effective means for marketing. Tailored marketing activities targeted at only the relevant audience can substantially decrease the cost of communication while boosting response rates. Companies should move more towards targeted activities in promoting their products and services, cutting down their marketing budgets while keeping and even improving their effectiveness (Peacock, 2005).

A high variety and frequent launches of new products and promotions can be a competitive advantage when trying to build a pioneering brand image in regular times. This however has led to many companies holding a portfolio of products and services that are bloated which includes too many, too few clients and little profits (Dess, Lumpkin and Taylor, 2004).

An economic downturn is an ideal time for rationalizing marketing portfolios and eliminating the unprofitable offerings, ultimately to save money and resources (David, 2002).. Companies can move towards using channels such as e-mail instead of eliminating their marketing communication all together. This guideline also applies even in the case of mass marketing, where companies should look for ways to optimize their media mix, investing in mass media that offers the best return on investment (Grahame, 2005).

2.6.7 Outsourcing

Outsourcing is the process of contracting out a business process, which an organization may have previously performed internally or which the company deems necessary or important, to an independent organization, where the process is purchase as service. An outsourcing deal may also involve transfer of the employees involved to the outsourcing business partner (Schiff and Schiff, 2008). Although, the definition of outsourcing includes both foreign and domestic contracting, the term is sometimes used exclusively referring to the former. The more clear term for this is off shoring, which can be described as a company taking a function out of their out of their business and relocating it to another country, whether the external country is physically offshore or not (David, 2002).

Outsourcing can also be referred to as sub-servicing. Outsourcing refers to the process of contracting to a third party (Grant, 1996). Organizations can manage costs by utilizing off shoring and outsourcing to variable costs while reducing fixed cost base, and tight control of external expenditures (Devine, Ealey and O'clock, 2008). Outsourcing may be considered an operational cost cutting measure when services and operations which the company may deem expensive and time consuming if they undertake them are lend out.

Optimizing staff utilization and outsourcing of organizations' non-core activities if cheaper can also reduce costs. Staff optimization by allocating the right amount of resources based on changing market demand and conditions is sometimes inevitable. However, companies should also look into maximizing their utilization, by allocating cross functional responsible (David, 2002). Out sourcing is another effective way of decreasing operational costs and complexities. For departments in which outsourcing is cheaper, companies should look for more activities to outsource (Grahame, 2005).

2.6.8 Customer Re-organization

From a pure profitability point of view, not all customers are equal, and, they should not be treated equally (David, 2002). Retention of high value and high potential customers are far more critical than individual mass customers, especially in times of economic downturn. Companies should focus their limited marketing budgets on getting, retaining and growing these customers as much as they can. At the other end of the spectrum is the below zero customers, who have negative impact on the company bottom line. Companies should also consider ways for selectively "firing" these customers, unless they have the potential to grow into profitable customers (Schiff and Schiff, 2008).

Times spend on unqualified leads and long sales closure cycles are significant inefficiencies in the utilization of sales staff, a very costly aspect of conducting business. Companies should focus on excellence in their sales activities, optimizing their leads generating activities, reducing times spend on lead list with limited potential, as well as processes in their sales cycles, to get the job done in minimum amount of time possible with minimum resources (Grant, 1996)

2.6.9 Technological Upgrade

Technology and software is evolving rapidly, giving users more time saving feature and faster processing proceeds. In most businesses, the rate of new software upgrade and advances in computing power requires business owners to plan for technology refreshes every few years. By practically planning for technology upgrades, business owners can ensure their staff has the tools to improve efficiency and deliver quality customer service and in turn reducing the operational costs (Dess, Lumpkin and Taylor, 2004).

Although most companies abandon their investment in technology altogether during harsh times, automation can mean lower cost of human resources, less paper use and faster operations, all resulting in substantial cost savings. Companies which can find ways to make better use of their existing information technology systems make minimal investments with substantial impact can create considerable cost savings through such efforts (David, 2002). Cash is, ultimately, the inventory of financial institutes, and as in all industries, effective management of cost of inventory results in decrease of costs. By optimizing levels of cash in automated teller machines and across branches as well as automating transactions as much as possible, banks can decrease cash handling maintenance cost as well as their opportunity costs (Cooper and Kaplan, 1991).

Over the years, most banks treated customer channel migration as a priority, seeking out means to decrease crowds at the branches as well as to reduce cost of services. With the downturn, this has become even more critical. The cost to serve a customer via the internet pales in comparison to branch service costs. Numerous methods i.e. loyalty program incentives and higher interest rates can be used to drive the migration of customers to lower cost channels (Dess, Lumpkin and Taylor, 2004).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the methodology, which was used to conduct the study. It covered the research design, the population of study, data collection and procedures and the method of data analysis.

3.2 Research Design

This research adopted a cross sectional descriptive survey design. Cross sectional descriptive survey design is a systematic, empirical enquiry into which the researcher does not have direct control of the independent variables as their manifestation has already occurred or because they inherently cannot be manipulated. In descriptive design, accurate data is easily gathered through observation, interviews and the use of questionnaires.

Cross sectional descriptive survey was appropriate because the population under study was small. It aimed to provide data on the entire population under study where all commercial banks in Kenya were selected. The design was appropriate because it provided an ample opportunity for detailed examination of the issues pertinent to the study.

3.3 Population of Study

A population is a well defined or a set of people, services, elements, and events, group of things or households that are being investigated. This definition ensures that population of interest is homogeneous. The target population was small and thus the study targeted all the forty three (43) commercial banks in Kenya (CBK, 2011).

This study was done with the assumption that the operational managers and assistant managers working for the commercial banks in Kenya will give the required information for the purpose of this study.

3.4 Data Collection

Questionnaires were used as primary data collection instruments. Some of the questions in the questionnaire were open ended to give the respondents complete freedom of response and know the suggestions they recommended. The rest of the questions were closed ended and these were designed to get the answers that the study needed to determine.

The questionnaire was divided into three parts. The first part included the demographic and operational characteristics designed to determine fundamental issues including the demographic characteristics of the subject under study. The second part focused on the cost drivers that affect the operational costs among the commercial banks in Kenya, while the third part focused on the cost management strategies that the commercial banks in Kenya can use to manage their operational costs.

The questionnaires were administered through drop and pick method. The researcher distributed the questionnaires among all the 43 commercial banks operating in Kenya. The questionnaires were collected after three weeks where the researcher followed by asking for the filled questionnaires from the respondents.

3.5 Data Analysis

The collected data were thoroughly examined and checked for completeness and consistency. This ensured that the questionnaires were completed as required. The data were then tabulated. After tabulation, the data were then coded to facilitate statistical analysis.

Statistical package for social sciences was used to analyze the strategies used by the commercial banks in Kenya to manage operational costs. Descriptive statistics such as frequency distribution, percentages and tables were used for data presentation.

CHAPTER FOUR

DATA ANALYSIS, FINDINGS AND DISCUSSION

4.1 Introduction

This chapter presents data analysis and interpretation, which are drawn from the objective of the study. The objective of this study was to determine the strategies used by commercial banks in Kenya in managing operational costs. The analysis is presented using tables and percentages. This chapter focused on data analysis, presentation, interpretation and discussion.

4.2 Response Rate

To understand the actual number of the respondents who answered and submitted back the questionnaires, the analysis of the response was conducted as follows;

Table 4.1: Response rate

Response	**Frequency**	**Percentage (%)**
Responded	39	91%
Not Responded	4	9%
Total	43	100%

Source: Field data (2012)

From table 4.1 it is clear that out of the 43 respondents who were issued with the questionnaires, 39 respondents (91%) actively participated in the study by answering and submitting back the questionnaires. It is indicated that only 4 respondents (9%) were unable to fill and submit the questionnaires for data analysis.

The analysis of the study therefore implied that majority of the respondents (91%) participated on the research study. The response rate was therefore good and sufficient to conduct the research study.

4.3 Organizational Demographics

The questions involved in this section were to help in determining the accuracy of the data collected by assessing the name of the organization, when it was established, the position and the department the responded is in and the period in which the responded has worked for the organization in relation to the research questions being examined.

4.3.1 Establishment of the organization

Table 4.2: Establishment of the organization

Years	Frequency	Percentage
60 years and above	3	8%
59 - 40 years	11	28%
39 - 20 years	14	36%
19 years and below	11	28%
Total	39	100%

Source: Research Data (2012)

The study sought to investigate when the organizations were established in Kenya. Table 4.2 above shows when the organizations were established as per the results given by the respondents. The table and figure indicates that 3 of the organizations (8%) were established 60 years and above, 11 of the organizations (28%) were established between

59-40 years, 14 of the organizations (36%) were established between 39-20 years and 11 of the organizations (28%) were established 19 years and below.

The analysis of the findings indicated that most of the commercial banks in Kenya have been operating for 20 years and above. This implied that the organizations had been in operation for many years and thus they could be in a position to adopt the cost management strategies due to experience gained in the market.

4.3.2 Respondent's working experience

The study sought to investigate the period in which the respondents have worked. Table 4.3 shows the working experience held by the respondents who participated in the research study. The table clearly indicates that 2 of the respondents (5%) had a working experience of below 3 years, 18 respondents (46%) between 3-6 years, 14 respondents (36%) between 7-10 years and 5 respondents (13%) has worked for 11 years and above.

Table 4.3: Working experience

Working experience	Frequency	Percentage (%)
Below 3 years	2	5%
3-6 years	18	46%
7-10 years	14	36%
11 years and above	5	13%
Total	39	100%

Source: Research Data (2012)

From the findings, majority of the respondents indicated that they have been working with their organization for within 3-6 years. This implied that the respondents have been working long enough for the commercial banks to give appropriate information required for the research study.

4.4 Extent of Effects of Cost Drivers for Commercial Banks in Kenya

4.4.1 Staff Salaries /Benefits

The study sought to investigate the extent to which staff salaries/benefits increases operational costs. As shown in table 4.4 above, 59% of the respondents expressed that staff salaries/benefits affected operational costs to a great extent for commercial banks, 31% to an average extent and 10% to a low extent.

Table 4.4: Effect of staff salaries/benefits on operational costs

Extent of the effect of staff salaries/benefits on operational costs	Frequency	Percentage (%)
Great extent	23	59%
Average	12	31%
Low	4	10%
Total	39	100%

Source: Research Data (2012)

The findings implied that the staff benefits/salaries increase the operational costs. The number of identifiable programs and the cost per program determines the number of employees required to work program. This in turn determines how much is to be spent on the employees as staff salaries/benefits and thus driving the operational costs.

4.4.2 The Number of Employees

The number of employees working in an organization affects its cost structure in terms of compensation they get after working. The respondents were asked the extent to which the number of employees in their organization increases operational costs. As shown in table 4.5, 72% of the respondents indicated that the number of employees in the organizations increased operational costs to a great extent for the commercial banks in Kenya, 21% to an average extent and 7% to a low extent.

Table 4.5: Effect of the number of employees on operational costs

Extent of the effect of number of employees on operational costs	Frequency	Percentage (%)
Great extent	28	72%
Average	8	21%
Low	3	7%
Total	39	100%

Source: Research Data (2012)

The findings of the study implied that the number of employees increase the operational costs as supported by the majority of the respondents (72%). The number of employees drives operational costs in terms of how much the organization is supposed to spend on employee remuneration.

4.4.3 Products Uniqueness

The study sought to investigate the extent to which the uniqueness of the products/services offered to the customers drives the operational costs. From the findings as indicated by table 4.6, 53% of the respondents indicated that the uniqueness of products/services offered to customers increase operational costs to a great extent for the commercial banks in Kenya, 31% to an average extent and 15% to a low extent.

Table 4.6: The extent of the effect of product uniqueness on operational costs

Extent of the effect of number of employees on operational costs	Frequency	Percentage (%)
Great extent	21	53%
Average	12	31%
Low	6	15%
Total	39	100%

Source: Research Findings (2012)

The findings of the study therefore implied that the uniqueness of products/services offered to customers' increase operational costs as supported by majority of the respondents (53%). The amount of unique products demanded by clients and the number of employees required for their production drives operational costs.

4.4.4 Investment in Highly Demanded Products/Services by Customers

The study sought to investigate the extent to which the highly demanded products by the customers increase the operational costs. From the findings as indicated by table 4.7, 82% of the respondents indicated that investment in highly demanded products and services increase operational costs to a great extent for the commercial banks in Kenya, 13% to an average extent and 5% to a low extent.

Table 4.7: Investment in highly demanded products/services by customers

Effect of the number of employees on operational costs	**Frequency**	**Percentage (%)**
Great extent	32	82%
Average extent	5	13%
Low extent	2	5%
Total	39	100%

Source: Research Findings (2012)

The findings of the study therefore implied that investment in highly demanded products/services increase operational costs as supported by majority of the respondents (82%). Investment in highly demanded products/services by customers requires for a research to determine the products/services demanded. Operational costs is therefore driven in terms of the research required to determine the products/services demanded by the customers, the number of the extra products demanded by the customer and the time taken to process the products.

4.4.5 Information Technology

The study sought to investigate the extent to which information technology requirements have led to the increase of operational costs. Table 4.8 shows that 44% of the respondents indicated that information technology increase operational costs for the commercial banks in Kenya, 38% to an average extent and 18% to a low extent.

Table 4.8: The extent of the effect of information technology on operational costs

The extent of the effect of information technology on operational costs	Frequency	Percentage (%)
Great extent	17	44%
Moderate extent	15	38%
Low extent	7	18%
Total	39	100%

Source: Research Findings (2012)

Information technology facilitates fast and effective execution of banking services/function. The cost driver in information technology would be the number of equipment required to work on a program and the number of staff who are specialized in the field of information technology to work on the programs. The finding therefore implied that investment information technology requirements can be considered as one of the cost drivers of operational cost though not to a great extent compared to the other cost drivers under the subject.

4.4.6 Quality of Products/Services Offered to Customers

The study sought to investigate the extent to which quality management for products and services offered to customers increases the operational costs. From the findings as indicated in table 4.9, the study found that 59% of the respondents indicated that quality of products and services offered to customers' increase operational costs for the commercial banks in Kenya, 26% to an average extent and 15% to a low extent.

Table 4.9: Quality of Products/Services Offered to Customers

Quality of Products/Services Offered to Customers	Frequency	Percentage
Great extent	23	59%
Average extent	10	26%
Low extent	6	15%
Total	39	100%

Source: Research Findings (2012)

Quality management attracts more customers and in return more income is generated for the organization. Quality management for the products and services also helps the organization in being competitive in the specific industry its operating in. this drives the cost of operation in terms of the number and costs of the unique process required for their production. The findings therefore implied that quality management for the products and services offered to customers is one of the cost drivers as supported by majority of the respondents (59%).

4.4.7 Strategic Positioning and Security

The study sought to investigate the extent to which the strategic positioning and security of both the business and its customers increases operational costs. From the findings, strategic positioning and security of the organizations sub-branches was considered to increase the operational costs the most. This is indicated in the table 4.10 where 77% of the respondents expressed that strategic positioning and security of both the business and its customers increases operational costs for commercial banks in Kenya, 18% agreed to an average extent while 5% agreed to a low extent.

Table 4.10: Effect of strategic positioning and security on operational costs

Effect of strategic positioning and security on operational costs	Frequency	Percentage
Great extent	30	77%
Average extent	7	18%
Low extent	2	5%
Total	39	100%

Source: Research Data (2012)

A good location increases an organization's income due to easy accessibility of the place by many customers. A good location also facilitates the security also facilitates the security of the organization. A good location with high security level attracts high demand which in turn increases the cost of the premises. The findings therefore implied that strategic positioning and security of an organization drives operational costs as supported by the majority of the respondents (77%).

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4.5 Cost Management Strategies

4.5.1 Mergers and Acquisitions

Table 4.12 shows the extent to which commercial banks use mergers and acquisition as a strategy for managing operational costs. The table and the figure presents that only 3% of the respondents expressed that they use mergers and acquisitions in managing operational costs to a great extent, 0% to an average extent and low extent and 97% not at all.

Table 4.12: Extent of using mergers and acquisition to manage operational costs

	Frequency	Percentage
Great extent	1	3%
Average extent	0	0%
Low extent	0	0%
Not at all	38	97%
Total	39	100%

Source: Research Data (2012)

Mergers and acquisition allows for cost management when the operational costs are consolidated and the banks portfolio is diversified. As per the research findings, majority of the respondents did not agree that mergers and acquisition is used as a cost management strategy. This is because the strategy involves the joining together of two independent organization which were operating separately initially and which may involve the consideration of other parameters before consolidating.

4.5.2 Organizational Restructuring

Table 4.13 shows the extent to which commercial banks use organizational restructuring as a strategy for managing operational costs. The table and the figure presents that 48% of the respondents expressed that they use organizational restructuring in managing operational costs to a great extent, 26% to an average extent and 26% to a low extent.

Table 4.13: Extent of using organizational restructuring to manage operational costs

	Frequency	Percentage
Great extent	19	48%
Average extent	10	26%
Low extent	10	26%
Total	39	100%

Source: Research Data (2012)

As per the research findings, majority of the findings agreed that restructuring is used as cost management strategy by commercial banks in Kenya. Restructuring involves reorganizing an organization where its composition and operations completely changes. Restructuring frequently results in elimination or replacement of departments and divisions causing permanent or temporary layoffs which results to cost savings for the organization.

4.5.3 Business Process Re-engineering

Table 4.14 shows the extent to which commercial banks uses business process re-engineering as a strategy for managing operational costs. The table and the figure presents that 69% of the respondents expressed that they use business process re-engineering in managing operational costs to a great extent, 26% to an average extent and 5% to a low extent.

Table 4.14: Extent of using business process re-engineering to manage operational costs

	Frequency	Percentage
Great extent	27	69%
Average extent	10	26%
Low extent	2	5%
Total	39	100%

Source: Research Data (2012)

Business process re-engineering eliminates inconsequential steps or allows for the use of less expensive resource for the execution of organization processes. This strategy allows for process redesign which enables it to move from its original way of performance and as a result it economizes the cost of operations that thus can be used in managing operational costs for commercial banks in Kenya. As per the study findings, this is supported by the majority of the respondents (69%) who agreed that business process re-engineering can be used to manage operational costs by the commercial banks in Kenya.

4.5.4 Consolidation of Business Functions

Table 4.15 shows the extent to which commercial banks use consolidation of business functions as a strategy for managing operational costs. The table and the figure presents that 64% of the respondents expressed that they use consolidation of business functions in managing operational costs to a great extent, 26% to an average extent and 5% to a low extent.

Table 4.15: Extent of using consolidation of business functions to manage operational costs

	Frequency	Percentage
Great extent	25	64%
Average extent	8	21%
Low extent	6	16%
Total	39	100%

Source: Research Data (2012)

Consolidation of business activities reduces operational redundancies and eliminates superfluous staff and administrative functions. It also eliminates replication of business activities across branches which create inefficiencies in operations. As per the study findings, this is supported by the majority of the respondents (64%) who strongly agreed that consolidation of business functions can be used to manage operational costs by the commercial banks in Kenya.

4.5.5 Rationalization of Staff Fringe Benefit

Table 4.16 shows the extent to which commercial banks use rationalization of staff fringe benefits as a strategy for managing operational costs. The table and the figure presents that 54% of the respondents expressed that they use rationalization of staff fringe benefits in managing operational costs to a great extent, 23% to an average extent and 23% to a low extent.

Table 4.16: Extent of using rationalization of staff fringe benefits to manage operational costs

	Frequency	Percentage
Great extent	21	54%
Average extent	9	23%
Low extent	9	23%
Total	39	100%

Source: Research Data (2012)

As per the research findings, majority of the respondents (54%) strongly agreed that rationalization of staff fringe benefits can be used in managing operational costs for commercial banks in Kenya. Rationalization of staff fringe benefits can be used in reducing staff operational costs where organizations enforce restrictions on personal use of corporate products/services. Organizations can find ways of decreasing cost son non-monetary benefits or free services which are not vital and would not necessarily create much dissatisfaction to employees.

4.5.6 Marketing Reduction

Table 4.17 shows the extent to which commercial banks use marketing reduction as a strategy for managing operational costs. The table and the figure presents that 28% of the respondents expressed that they use marketing reduction in managing operational costs to a great extent, 39% to an average extent and 33% to a low extent.

Table 4.17: Extent of using marketing reduction to manage operational costs

	Frequency	Percentage
Great extent	11	28%
Average extent	15	39%
Low extent	13	33%
Total	39	100%

Source: Research Data (2012)

Tailored marketing activities targeted at only the relevant audience can subsequently decrease the cost of communication while boosting response rate and at the same time cutting down on the marketing budget. The research findings revealed that most of the respondents (39%) agreed to an average extent that marketing reduction can be used as a strategy for managing operational costs for commercial banks in Kenya.

4.5.7 Outsourcing

Table 4.18 shows the extent to which commercial banks use outsourcing as a strategy for managing operational costs. The table and the figure presents that 41% of the respondents expressed that they use outsourcing in managing operational costs to a great extent, 36% to an average extent and 23% to a low extent.

Table 4.18: Extent of using outsourcing to manage operational costs

	Frequency	Percentage
Great extent	16	41%
Average extent	14	36%
Low extent	9	23%
Total	39	100%

Source: Research Data (2012)

Outsourcing can be used as an effective way of managing operational costs and decreasing complexities where an organization maximizes staff utilization by allocating cross functional responsibilities. This is supported by majority of the respondents (41%) who strongly agreed that commercial banks in Kenya use outsourcing as one of the strategies for managing operational costs.

4.5.8 Customer Re-organization

Table 4.19 shows the extent to which commercial banks use customer re-organization as a strategy for managing operational costs. The table and the figure presents that 33% of the respondents expressed that they use customer re-organization in managing operational costs to a great extent, 36% to an average extent and 31% to a low extent.

Table 4.19: Extent of using customer re-organization to manage operational costs

	Frequency	Percentage
Great extent	13	33%
Average extent	14	36%
Low extent	12	31%
Total	39	100%

Source: Research Data (2012)

The research findings showed that the majority of the respondents (36%) agreed to an average extent that customer reorganization can be used as a strategy to manage operational costs by commercial banks in Kenya. Customer re-organization facilitates costs savings when customers with a negative impact on the organization are avoided. Time spent on unqualified leads is also avoided which allows for efficient utilization of organizations sales staff and thus facilitates cost management.

4.5.9 Technological Upgrade

Table 4.18 shows the extent to which commercial banks use technological upgrade as a strategy for managing operational costs. The table and the figure presents that 56% of the respondents expressed that they use technological upgrade in managing operational costs to a great extent, 26% to an average extent and 18% to a low extent.

Table 4.18: Extent of using technological upgrade to manage operational costs

	Frequency	Percentage
Great extent	22	56%
Average extent	10	26%
Low extent	7	18%
Total	39	100%

Source: Research Data (2012)

Technological upgrade facilitates the efficient flow of work within business functions by ensuring that staff members have tools of improving efficiency and deliver quality customer service and in turn reduces operational costs while maximizing profits. This is supported by the majority of the respondents (56%) who agreed to great extent that technological upgrade can be used as a strategy in managing operational costs.

4.6 Discussion

The study focused on business process re-engineering, consolidation of business functions, mergers and acquisition, restructuring, rationalization of staff fringe benefits, marketing reduction, outsourcing, customer re-organization and technological upgrade in determining strategies which commercial banks in Kenya can use to manage operational costs. The analysis provides some interesting insight on strategies used by commercial banks in managing operational costs. Through answering the questionnaires the respondents had a chance to express their sentiments towards each of the variables to the best of their knowledge.

The results from the study indicated that the commercial banks in Kenya use business process re-engineering in managing operational costs. Majority of the respondents explained that business process re-engineering involves process redesign which allows for a move from the original process design which allows for ways to decrease the cost of operations through economizing process designs. This concurs with Stacey (2003), who stated that business process re-engineering allows for the introduction of complete new ways of doing things which results in cost management. Commercial banks in Kenya should therefore use business process to manage operational costs as it focuses on the banks business process, steps and procedures that govern how resources are used efficiently and effectively.

Replication of activities across branches usually creates utilization inefficiencies in operations. Consolidating certain functions via utilization of centralized approach results in significant operational savings. Majority of the respondents indicated that consolidation of business functions is used in managing operational cost. This allows for the closure of unprofitable channels thus saving operational costs. The findings are in agreement with the studies of Grant (2001) who stated that consolidation improves communication between business functions, such as production and marketing and achieves costs savings by decreasing head count, processes and consolidation of systems.

Restructuring allows for employees reorganization where some of the employees who may be redundant may be permanently or temporally released. This is in line with the studies of Gandolfi (2009) who termed restructuring as beneficial in terms of increased operational efficiency and increased productivity. Commercial banks should however facilitate clear, open communication when restructuring that enables clarity and accountability.

In any organization, staff members are usually considered as the company's capital and thus their payrolls are usually considered as the biggest expense. Rationalization measures are therefore considered to decrease operational costs when strict measures are put when it comes to using corporate services. The respondents also felt that rationalization of staff fringe benefits can be used in managing operational cost. This is supported by Peacock (2005) who states that rationalization of staff fringe benefits allows for improved operations and profit enhancement.

From the findings, majority of the respondents felt that marketing respondents reduces operational cost. Marketing reduction allows for tailored marketing where the relevant audiences are the only ones targeted thus avoiding the extra costs which could have been spend in mass market. This also boosts the customers' response rate and thus productivity is enhanced. This is in agreement with David (2002) studies who stated that companies should move more towards targeted activities in promoting their products/services which leads to cutting down their marketing budgets and even improving their performances.

From the study, the results indicated that majority of the respondents felt that technological upgrade is used in managing operational cost. The respondents indicated that lack of integration of technology into their work slowed down the banks functions and thus increasing operational costs. This is supported by David (2002) who states that companies can find ways to make better use of their existing information technology system which have subsequent impact on cost savings. Commercial banks in Kenya should therefore adopt technological upgrade to manage operational costs as it allows for quality customer service and faster work delivery.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

In this chapter, a summary of the findings from chapter four was discussed, conclusions drawn, recommendations of the study made based on the objectives of the study. Challenges of the study were also established. The main objective of this study was to determine the elements that drive operational costs and the strategies that can be adopted by commercial banks in Kenya to manage the operational costs.

5.2 Summary of the Findings

Cost management is a fundamental aspect for productivity of any organization. Operating any business with cost management in mind helps avoid certain pitfalls which may occur. Based on the study finding, the study drew that effective management of cost is usually facilitated by well defined operational procedures. Cost management cannot be used in isolation; projects must be organized and tailored with strategy in mind as well as the cost items.

Technology facilitates effective execution of banking services/function. The use of computer networks such as internet helps in fast exchange of information for the banks departments as well as with other stakeholders. This leads to fast and effective services. Proper utilization of technology facilitates speeding up of service provision. Technology is therefore a major factor that affects operational costs for commercial banks in Kenya.

The location of the commercial banks affects its accessibility as well as its security and that of its clients. A good location would lead to many clients visiting the banks because of ease of accessibility. Security of the clients, employees and the commercial banks will

be ensured be ensured if the location is good. Lastly, proximity to the source of materials needed in the commercial banks will lead to reduced costs. Location is therefore a major factor that affects operational costs for the commercial banks in Kenya.

In light of quality management, organizations are required to offer quality products/services to their customers. Quality management attracts more customers and this result to more income for the organization. The uniqueness of the products/services offered to the customers also enables an organization to be more competitive in the specific industry its operating in. The quality of products/services, investment in highly demanded products/services and the uniqueness of the products/services offered by the commercial banks in Kenya therefore affects their operational costs.

The number of programs operating in an organization determines the number of employees the organization hires. In return the number of people recruited determines how much the organization spends on the staff salaries and benefits given to them. The number of employees is therefore a major factor that affects the operational costs for commercial banks in Kenya.

Restructuring and rationalization of staff fringe benefits can be used to manage operational costs. Restructuring can either be through downsizing or retrenching which allows for the reorganization for the employers undertaking and elimination of the redundant employees. Rationalization of the staff fringe benefits decreases operational costs by focusing on the non monetary benefits or free services which may not be vital and would not necessarily create as much dissatisfaction to employees if eliminated. Rationalization of the staff fringe benefits and restructuring can therefore be considered as strategies which can be used to manage operational costs for commercial banks in Kenya.

5.3 Conclusion

The main purpose of this research was to determine the strategies used by commercial banks in Kenya to manage operational costs. The study sought to answer two main questions: Firstly, to establish the cost drivers among the commercial banks in Kenya and secondly, is to determine the strategies that can be adopted by the commercial bank in Kenya to manage the operational costs.

The research findings show that the commercial banks in Kenya realize the importance of managing operational costs so as to improve productivity. It was indicated that in order to manage the operational costs, the commercial banks need to identify the specific cost items which drive the operational costs since different cost items are managed using different cost management strategies. The study established that the cost drivers affect the cost structures among the commercial banks in Kenya in varying intensities. The cost drivers identified to affect the cost structure the most included strategic positioning and the security of the branch sub-branches, investments in highly demanded products/services by the customers and the number of employees in the organization. The other cost drivers found to affect an organization's cost structure included staff salaries/benefits, quality and uniqueness of the products/services offered by the banks, information technology requirements and advertisement needs.

The research findings also showed that a successful cost management practices are meant to provide a framework to understand and control the operational costs within the commercial banks in Kenya. However, the findings indicated that the commercial banks in Kenya different commercial banks preferred different cost management strategies over others, for instance, the research findings indicated that mergers and acquisition was only used by one bank. The cost management strategy which was found to be highly used by the commercial banks in Kenya was process re-engineering. The other cost

management strategies used included consolidation of business functions, rationalization of staff fringe benefits, restructuring, outsourcing and customer reorganization. Advertisement reduction was found to be one of the least used cost management strategies to be used by the banks.

5.4 Recommendations for Policy and Practice

Commercial banks in Kenya should utilize the benefits of technology. They should invest in up to date equipment and computerized programs that give updated information on the banks operations and products/services offered. Effective and strategic application of this recommendation will support realization of fast banks operations and reduced operational costs for the commercial banks. Since technology is dynamic, commercial banks should from time to time upgrade their equipment as well as continually train their staff to be able to efficiently and effectively get the best out of the technology available to them.

When it comes to the location, commercial banks should choose to set up their premises in strategic location. The location should be well accessible to their clientele as well as being in proximity of the sources of materials needed to run the commercial banks. Among other factors security should also be considered to be vital when selecting a good location for the commercial banks. Location and proximity to markets are important for the commercial banks.

Commercial banks should also utilize the benefits of customer reorganization. Customer re-organization allows for the focus and retention of high value and high potential customers. In customer reorganization, the customers who have a negative impact on the organization are usually selectively fired thus saving the costs which could have been

spent on them. Customers reorganization therefore allows for high productivity and cost saving.

In regards to marketing reduction, commercial banks should practice tailored marketing where relevant audience is targeted unlike mass marketing. Tailored marketing substantially decreases the cost of communication and boosts response rate. Commercial banks should also consider consolidation of business functions which helps in reducing operational redundancies and elimination of extra staff and administration functions. The reduction on the number of facilities eliminates the replication of activities across the business marketing reduction and consolidation of business function can therefore be considered as major strategies which commercial banks can use in managing their operational costs.

In regards to rationalization of staff fringe benefits, commercial banks should take action and put more restrictions on personal use of corporate services. Although these services are considered to have a negative impact employee's morale, they usually make a huge impact on operational cost. Rationalization of staff fringe benefits is therefore a major strategy which commercial banks in Kenya can use in managing their operational costs.

5.5 Limitations of the Study

The study only explored on a few major factors that were addressed by specific objectives and cannot be fully relied upon to be the only factors affecting operational costs or the only strategies which can be used in managing operational costs for commercial banks in Kenya. The delay in collection of data as respondents took more time than had stipulated was the other challenge encountered.

The other limitation of the study was that it was limited to commercial banks in Kenya only and this may not provide appropriate information to banks with foreign subsidiary

branches. The study should have been broad enough to bring on board foreign banks in order to show global banking industry trended. Secondly, the study focused its attention on operational costs disregarding the other organizational costs. It would have been of great value to obtain information from the other foreign banks.

5.6 Suggestions for Further Study

The study investigated few major strategies used by commercial banks in Kenya to manage the operational costs which was not enough since there more strategies which can be used. Suggestion for further study is therefore encouraged to facilitate establishment of other factors that affect operational costs and also other strategies which can be used in managing the operational costs.

Researchers can also conduct further study to establish the strategies used by foreign banks in managing their operational costs. This will provide proper framework to both the decision makers and policy formulators in the banking industry internationally. Using a sample population where the subject of study is big is encouraged to avoid the delay when collecting data.

The results of this research prompt new possible studies. Further study should be carried out to establish ways through which cost management has helped in improving the productivity of the commercial banks in Kenya. A further study should be carried out to determine the productivity and the financial performance of the commercial banks in Kenya through cost management.

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APPENDICES

Appendix I: Letter of Introduction

Obiga Ann Mercy Atieno,
School of Business,
University of Nairobi,
P. O. BOX 30197,
NAIROBI.

September, 2011.

Dear respondents,

RE: REQUEST FOR RESEARCH DATA

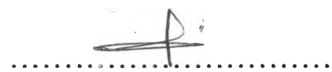
I am a Postgraduate student at the University of Nairobi, School of Business. In partial fulfillment of the program Masters in Business Administration (MBA) requirement, I am undertaking a management research project titled.

Strategies used by commercial banks in Kenya in managing operational costs.

You have been selected as part of the study. This is to request you to assist me to collect the data by filling out the attached questionnaire. The information you will provide be used exclusively for academic purposes. My supervisor and I, assure you that the information you will give, will be treated with strict confidentiality. A copy of the final report will be availed upon request.

Your cooperation will be highly appreciated, thanking you in advance.

Yours Faithfully,



....

Obiga Ann Mercy Atieno — Dr. V. Machuki

MBA Student — Supervisor

Appendix II: Questionnaire

Section A: Organizational Demographics

What is the name of the organization?...

When was the organization established?...

When did you join the organization (Year)?...

Section B: Cost Drivers

1. To what extent have the staff salaries/benefits increased operational costs in your organization?

   - Great extent
   - Average
   - Low
   - Not at all

2. To what extent has the number of employees in your organization affected the organization's cost structure?

   - Great extent
   - Average
   - Low
   - Not at all

3. To what extent does the uniqueness of products/services offered to the customers increase the operational costs in your organization?

  - Great extent
  - Average
  - Low
  - Not at all

4. To what extent does your company invest in highly demanded products/services by the customers?

  - Great extent
  - Average
  - Low
  - Not at all

5. To what extent has the information technological requirement in your organization led to increased operational costs?

  - Great extent
  - Average
  - Low
  - Not at all

6. To what extent has the quality of products/services offered by your organization increased the operational cost?

  - Great extent
  - Average
  - Low

- Not at all

7. To what extent has the strategic positioning and security of your organization(s)' sub-branches led to increased costs?

- Great extent
- Average
- Low
- Not at all

8. To what extent has the advertisement needs for your organizations led to inflated costs?

- Great extent
- Average
- Low
- Not at all

Section C: Cost Management Strategies

9. To what extent does your organization adopt business process re-engineering to manage the operational costs in your organization?

- Great extent
- Average
- Low
- Not at all

10. To what extent does your organization adopt consolidation of business functions as a strategy for managing the operational cost?

- Great extent
- Average
- Low
- Not at all

11. To what extent has your organization adopted mergers and acquisitions as an operational cost management strategy?

- Great extent
- Average
- Low
- Not at all

12. To what extent does your organization adopt restructuring cost management strategy to reduce the organization's operational costs?

- Great extent
- Average
- Low
- Not at all

13. To what extent has your company adopted rationalization of staff fringe benefit as strategy of managing the operational costs in your organization?

- Great extent
- Average
- Low

14. To what extent does your organization adopted advertisement reduction as a strategy of reducing the operational costs?

- Great extent
- Average
- Low
- Not at all

15. To what extent does your organization adopt outsourcing as a strategy to manage the operational costs?

- Great extent
- Average
- Low
- Not at all

16. To what extent does your company adopt customer re-organization cost management strategy so as to cut costs?

- Great extent
- Average
- Low
- Not at all

THANK YOU

Appendix III: Commercial Banks in Kenya

African Banking Corporation

Bank of Africa Kenya Ltd

Bank of Baroda

Bank of India

Barclays Bank of Kenya

CFC Bank Ltd

Chase Bank

Citi Bank

Credit Bank Ltd

Diamond Trust Bank

Commercial Bank of Africa Ltd

Consolidated Bank of Kenya Ltd

Co-operative Bank

Development Bank of Kenya

Dubai Bank of Kenya Ltd

Eco-Bank Ltd

Equatorial Commercial Bank Ltd

Equity Bank

Family Bank

Fidelity Commercial Bank

Fina Bank

First Community Bank

Giro Bank

Guardian Bank

Gulf African Bank

Habib Bank Ltd

Housing finance

Imperial Bank Ltd

Investment and Mortgages

Kenya Commercial Bank

K-Rep Bank

Middle East Bank

National Bank of Kenya

NIC Bank

Oriental Commercial Bank

Paramount Universal Bank Ltd

Prime Bank Ltd

Southern Credit Corporation

Stanbic Bank Ltd

Standard Chartered Bank

Trans-National Bank

UBA Bank

Victoria Commercial Bank Ltd

Source: Government of Kenya (2011), *The Central Bank Act: Cap 489.* Nairobi, CBK.