

**RISK MANAGEMENT STRATEGIES USED BY EQUITY BANK
LTD TO ENHANCE PERFORMANCE**

BY

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DECLARATION

I declare that this research project is my original work and has not been presented to any other university for the award of a degree.

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

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DEDICATION

This research project is dedicated to all my family members especially my dear parents who were always there for me for their inspiration, support, encouragement and understanding throughout the research period.

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LIST OF ABBREVIATIONS/ACRONYMS

EAR:	Earning at Risk
EBS:	Equity Building Society
MPT:	Modern Portfolio Theory
RIM:	Risk and Insurance Management Society
USA:	United States of America
VAR:	Value at Risk

ABSTRACT

This study aimed to identify the risk management strategies implemented by Equity Bank and how those strategies have helped improve their performance. This study was a case study since the unit of analysis was one organization and the purpose was to establish the risk management strategies used by Equity bank to enhance performance for competitive advantage in the banking industry. The study aimed at getting detailed information regarding risk management strategies used by equity bank to enhance its performance. Primary data was collected using a self-administered interview guide. The respondents of this study were five senior managers of the bank. Data was analyzed using content analysis. The study revealed that risk occurrence has been a common phenomenon with the bank, that risk management is a key aspect in determining the performance of the equity bank. It was established that risk management enables the organization to classify its customers for better service, as close attention is given towards each and every customer to build their confidence. The risk management strategies that are used by Equity bank include risk control and risk financing. Risk control includes risk aversion, risk homeostasis, decision analysis and trade off analysis whereby risk financing involves risk retention and risk transfer. Retention is the deliberate acceptance of risk because it is low enough in probability to be reasonably assumed without impacting the development effort. Transfer can be used to reduce risks from one area of design to another where a design solution is less risky. The findings revealed that equity bank has adopted pricing strategy that takes into account the market inflation tendencies which are laid out in bank's contractual documents and tariffs. Market intelligence and research has also been conducted to check on the inflation trends to help mitigate such risks. The bank also manages through analysis the ability of borrowers and potential borrowers to meet interest and principal repayment obligations by obtaining collateral and corporate guarantees which are considered necessary and it has also adopted a Debt Recovery Unit which is in charge of follow-up and collections. The bank has access to diverse funding base that are raised mainly from deposits and share capital. The study recommended that bank should come up with effective risk management strategies which focus on the needs and wants of the customer towards building their confidence. Identified risks should be dealt with appropriately before their effects spill over to the organization clients. Managers should be able to identify the dynamic risks of the customer in order to keep abreast with the changing threats that are likely to impact on the performance of the bank. Equity bank has adequate capital which enables them to contain and manage risks through, fixed exchange rates, stable interest rates, capital controls, and oligopolistic banking markets which enhance profitability from low risk business, thus ability to overcome the effects of the equity risks. From the study it is evident that risk management is a key aspect in determining the bank performance. On what a bank can do to improve on the risk management strategies, it should adopt integration approach where they integrate human-resources systems into the strategic plan, it should also identify, assess, plan and implement the risk management strategies and keep records on the risk retention strategies so as to be able to follow track of all the risks and effectively report procedures on the risk occurrence.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Humans have been managing risk ever since, taking the opportunity out of risk and taking the risk out of opportunity is natural. However, making that process explicit, systematic and logical risk management only really began with the coming of probability counter thought. Further uncertainty arises in the area of operational risk due to the value of economic intangibles such as goodwill, and the volatility of interrelationships amongst the factors determining each aspect of risk and opportunity. Both the value of economic intangibles and volatility of interrelationships have been increasing rapidly over the last ten years (Anderson, 2006).

Risk and economic activity are inseparable and every business decision and entrepreneurial act is connected with risk (Stenchion, 1997). This applies also to business of banking sector as they are also facing several and often the same risks as other companies. In a real business environment with market imperfections they need to manage those risks in order to secure their business continuity and add additional value by avoiding or reducing transaction costs and cost of financial distress or bankruptcy (Stenchion, 1997)

Scholars of modern theory assert that for a large class of financial problems a separate analysis of actuarial and financial risks is inappropriate (Markowitz, 1952). This theory can be applied to banking institutions if there are risks with respect to default,

exchange rates, inflation and other risks which the financial institutions face. Game theory asserts that any decision problem where the outcome depends on the actions of more than one agent, as well as perhaps on other facts about the world there is need to understand what rational agents do in such situations Baird Gertner (2004). Contingency theory by Collier and Mark (2006) asserts that at the top level of the control system, the basic structures of risk management appear to be common across large organisations. At the detailed level, however, the structures are fine tuned to respond to specific risk management needs and environmental pressures. Further the theory asserts that external political uncertainty acts as an important driver of risk management because national policy influences how risks are prioritised, while locally elected members determine the resources available for control of risks.

Given these features, risk management remains more of an art than a science, despite the growing body of literature classified as risk management. In terms of quantitative work, substantial progress has been made. The basic principles of risk management are simple but lend themselves to elegant theories where data and process can be brought together in specialist niches. Similarly, there is a growing body of methodologies and case studies, which demonstrate how various risk management approaches can be used to bring structure to the management effectiveness and performance. This is in response to the mounting appreciation of the value that systematic management of risk provides, even in areas where reliable quantitative data does not exist (Grabowski, 2009)

Risk management has been recognized as a valuable discipline within various activities for some time, even if different terminology has been used. These range

from nuclear energy to policing initiatives. A particularly strong tradition has developed in areas where there is sufficiently reliable data to use specific approaches to produce useful quantitative results. Momentum has been building in applying the same principles in operational risk management, where data is less reliable or is unavailable, and subjective judgment is used to provide more qualitative assessments (Kowert, 1997)

While there has been steady progress in areas such as environmental care, various events around the world have accelerated the use of a systematic approach to the management of potential future events, while these events were sufficiently shocking at a national level to promote the advent of recognized operational risk management processes, at an organization level localized shocks caused similar demands to put risk management systems in place.

A major feature of risk management as it is used by line managers in both private and public sector organizations rather than vocational specialists is the degree of judgment involved. Usually the critical factor in being a good manager of risks for these decision-makers is not the rational reason for doing one thing rather than another but how each choice is felt. In the absence of complete or reliable quantitative data, and under time pressure, they resort to using intuition to evaluate cause and effect (Alibaba and VazirZanjani, 2009)

Banking sector notably Equity bank limited are prone to a number of risks which need proper risk management strategies where the probability of a loss that may be incurred by the bank can be mitigated by using risk mitigation techniques or imposing

limits to transactions that may generate risk, depending on the variability of controllable risks over time, risks of loss which cannot be predicted by using any risk measurement and mitigation techniques or by implementing exposure limits, and which is realized when they emerge (Porter, 2008b).

1.1.1 The Concept of Risk

According to (Sayers, 2002) Risk can be defined as a combination of chances of a particular event, with the impact that the event would cause if it occurred risk therefore has two components the chance or probability of an event occurring and the impact or the consequences of an event may be either desirable or undesirable. Risk therefore can be defined simply as the probability of occurrence of undesired event or probability of a hazard contributing to a potential disaster which involves consideration of the vulnerability of the hazard (Stenchion, 1997)

Risk is an inevitable and ever present element throughout life; from conception through to the point at the end of life when we finally lose our personal battle with life threatening risk. Therefore, risk assessment process includes all risks and risk/revenue trade off concerning management of such happenings. It includes the determination of the extent of controllability of risks. Managing risk is an effective technique for minimizing undesirable effects of risks and optimizing the benefits of risky situations (Essinger and Rosen, 2006). Chapman and (Ward, 1997) describe the aim of risk management as process enhancement that is established through systematic identification, evaluation and mitigation of project risks.

1.1.2 Risk Management Strategies

Risk management strategies refers to the identification, assessment, and prioritization of risks to avert the effect of uncertainty on performance, whether positive or negative followed by coordinated and economical application of resources to minimize, monitor, and control the probability and/or impact of unfortunate events (Hubbard and Douglas 2009) or to maximize the realization of opportunities resulting to an organizational performance. There are varied methods available for the banks to control the risks,

Risk management strategies involve risk control and risk financing. Risk control includes risk aversion, risk homeostasis, trade off analysis, decision analysis, insurance models and repair & maintainability issues. On the other hand risk financing includes risk retention and risk transfer. Retention is the deliberate acceptance of the risk because it is low enough in probability to be reasonably assumed without impacting the development effort. Transfer can be used to reduce risks from one area of design to another where a design solution is less risky (Crockford, 2006)

1.1.3 Organizational Performance

According to (Richard, 2009) Organizational performance comprises the actual output or results of an organization as measured against its intended outputs or goals and objectives. Organizational performance involves the recurring activities to establish organizational goals, monitor progress toward the goals, and make adjustments to achieve those goals more effectively and efficiently. Specialists in many fields are concerned with organizational performance including strategic planners, operations,

finance, legal, and organizational development, it's the ability of an organization to fulfill its mission through sound management, strong governance and a persistent rededication to achieving results. Effective nonprofits are mission-driven, adaptable, customer-focused, entrepreneurial, outcomes oriented and sustainable.

Awareness of risk is growing and risk management is increasingly seen as a critical practical discipline in enhancing organizational performance (Teach, 2007). Risk management framework is important for financial institutions all over the world. In conjunction with the underlying frameworks, basic risk management process that is generally accepted is the practice of identifying, analysing, measuring, and defining the desired risk level through risk control and risk transfer, effective measures taken to avert the effects of risks will lead to organizational performance. Hambrick and Cannella (1989) stated without successful implementation, a risk management strategy is but a fantasy. In many companies, more particularly in U.S.A and Europe focus mainly to setting strategy on the formulation of a new risk management on organizational performance. However, a good formulated risk management strategy does not automatically mean that the company achieves the objectives as set and gains organization performance. To ensure achievement of organizational objectives, the formulated strategy needs to be implemented at all levels of the organization. Implementing a strategy means putting the strategy to action to effectively manage all risks that the organization is facing.

1.1.4 Equity Bank Limited

Equity Bank was founded as Equity Building Society (EBS) in October 1984 and was originally a provider of mortgage financing for the majority of customers who fell

into the low income population. Having been declared technically insolvent in 1993, Equity's transformation into a rapidly growing microfinance and then a commercial bank is widely considered to be an inspirational success story. Currently, Equity Bank has more than 8 million customers making it the largest bank in terms of customer base in Africa and having nearly half of bank accounts in Kenya. Equity Bank retains a passionate commitment to empowering its clients to transform their lives and livelihoods. Through a business model that is anchored on access, convenience and flexibility, the Bank has evolved to become an all inclusive financial services provider with a growing pan African footprint.

Equity Bank provide various services to their clients these includes Equity agency, An Equity Agent therefore is a commercial entity that has been contracted by Equity Bank and approved by the Central Bank of Kenya to provide specific services on behalf of the bank. This entity has been equipped with the skills necessary to provide basic banking services according to standards set by the Bank. Besides Equity bank also provides safe custody services to their clients, it offers loan facilities to their clients at a cost, online banking, pay bills, mobile banking and mortgage facilities. The bank has continued to consolidate its position in Kenya, as at the end of February 2014 the bank had 8 million customers and 106 branches. (Carey, 2001) provides empirical evidence that building a branch network enables a firm to favourable compete due to increased proximity and resulting convenience which works towards reducing the risk occurrence.

Equity bank has also aggressively expanded to the Great Lakes region, where it intends to replicate its Kenyan model. Equity bank also aims at further growing its

market share by increasing its stake at Housing Finance and acquiring the government's 23% stake in National Bank. Because of these successful approaches by equity bank, Kenya's banking industry is currently led by two indigenous banks, Equity Bank and Kenya Commercial Bank. Equity bank has employed efficiency in decision making style, networking and strategic participation that has boosted its progress in managing all risks towards the realization of corporate success.

1.2 Research Problem

Risk is inherent in every economic activity and every organization has to manage it according to its size and nature of operation it would be assumed that risk management and internal control systems will vary from one organization to another based on their size or industry sector. It is therefore logical to assume that every business organization has put in place a strong risk management structure and internal control systems to help achieve its goals. These are fundamental to the successful operation and day to day running of a business and assist a company in achieving its objectives. Risk may affect many areas of activity, such as strategy, operation, finance, technology and environment. In terms of specifics, it may include, for example, loss of key staff, substantial reductions in financial and other resources, severe disruptions to the flow of information and communication, fires or other physical disasters, leading to interruptions of business and or loss of records. More generally, risk also encompasses issues such as fraud, waste, abuse and mismanagement.

Despite risks that face financial organizations, Equity bank's performance has improved which is evidence through strategic growth by successfully making acquisitions like the purchase of the retail business arm of the Industrial development bank, acquisition of the 20% of the housing finance and 100% acquisition of Uganda microfinance limited, moreover Eguity bank has increased its state in the housing finance to 24.9% through a rights issue (Equity Bank, 2007) this could be attributed to its risk management programs hence the need to find out what these risk management strategies are.

Previous researchers have concentrated on strategic management and internal control systems in the financial sector, (Siayo, 2010) did a study on the strategic management and internal control systems in the financial sector, his findings revealed that the structure of the organization ensures independent risk reporting, concluding that the group's risk management has the overall responsibility for risk management and internal control for assessing and reporting the company's overall risk situation. (Osna, 2006) did a study on the banks performance and credit risk management, the findings of his study revealed that there is a significant relationship between bank performance in terms of profitability and credit risk management in terms of loan performance.

In Germany, Henschel (2008) found in his study that two thirds of the banking institutions were not able to identify and measure the influence and impact of their business risks on their business. Consequently, around 40% of the surveyed banks did not identify their business risks and in addition to that 64% did not evaluate their risks properly. A study conducted by (Kimani, 2011) on fraud risk assessment plan for

Barclays Bank of Kenya identified theft and use of lost or stolen documents, use of counterfeit cards, bribery and conflicts of interest, misuse of company assets, theft of confidential information, cheque fraud and fund transfers, Travel and Entertainment fraud and money laundering. These studies did not reveal any risk management strategies used by the Equity Bank, thus leaving a research gap. The study thus sought to fill this gap by addressing the following questions, what are the risk management strategies used by Equity Bank to enhance performance?

1.3 Research Objectives

The objectives of this study were to:-

- i. To determine the risk management strategies used by Equity Bank
- ii. To establish the effects of risk management strategies on the performance of Equity Bank

1.4 Value of the study

The study will be a source of reference material for future researchers on other related topics; it would also help other academicians who undertake the similar topic in their studies. The study will also highlight important relationships that require further research on the risk management strategies used by the financial institutions. The study will contribute to theories already put down on risk management and the traditional methods to risk management, banks have successfully applied modern theories to manage their operations which would otherwise enhance exposures to risks. Unfortunately, however, risk remains the largest threat facing most banks; the

practical application of these theoretical models to effectively manage risk will enhance effective risk control to the financial institutions.

The findings of this study would be beneficial to the firms participating in the banking institution market since it would point on the risk management strategies and thus will aid them in assessing the performance in the financial market. The study finding would give a guide on the requirements by the banking institutions to control fraud and other risks associated with cash.

This study will be very valuable to the policy regulators like Central Bank of Kenya considering the pivotal position played by Equity Bank in the Kenyan banking industry. Other regulators who may be interested in Equity Bank case study include Kenya Bankers Association and Capital Markets Authority.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter presents literature reviewed on the risk management strategies used by the banking institutions. The first section gives the theoretical foundations of the study. The second section discusses the risk management strategies and the performance.

2.2 Theoretical Foundation of the Study

This chapter is about the theoretical background of the thesis. Theories about risk, risk management are elaborated in this section of the study. The study is based on modern portfolio theory, game theory and value at risk theory

2.2.1 Modern Portfolio Theory

Modern Portfolio theory is a mathematical formulation of the concept of diversification in investing, with the aim of selecting a collection of investment assets that has collectively lower risk than any individual asset. This is possible, because different types of assets often change in value in opposite ways. For instance, to the extent prices in the stock market move differently from prices in the bond market, a collection of both types of assets can in theory face lower overall risk than either individually. But diversification lowers risk even if assets' returns are not negatively correlated indeed, even if they are positively correlated.

The main proponent of the Modern portfolio theory was (Markowitz, 1952) the theory asserts that for a large class of financial problems a separate analysis of actuarial and financial risks is inappropriate. This theory can be applied to banking institutions if there are risks with respect to default, exchange rates, inflation and other risks which the financial institutions face.

The portfolio theory plays a pivotal role in explaining the need for the banking institutions to take appropriate measures to fully perform and maintain an effective, independent and strong risk management function within the context of an institutional risk culture constituted by the participation of personnel at all levels.

2.2.2 Game Theory

Game theory which was founded by Baird (2004) and it asserts that any decision problem where the outcome depends on the actions of more than one agent, as well as perhaps on other facts about the world there is need to understand what rational agents do in such situations. The theory further asserts that there should be specific ways in which strategic managements among economic agents produce outcomes with respect to the preferences utilities of those agents, where the outcomes in question might have been intended by none of the agents. Financial institutions risk strategies are the practices of the executive risk committee being responsible for preparation of risk management strategies and policies to be followed by the financial institutions, submission of such strategies and policies for approval and monitoring of implementation thereof is vital for effective risk management as the theory holds.

2.2.3 Contingency Theory

The main proponents of the theory are Collier and Mark (2006). Contingency theory asserts that at the top level of the control system, the basic structures of risk management appear to be common across large organisations. At the detailed level, however, the structures are fine tuned to respond to specific risk management needs and environmental pressures. Further the theory asserts that external political uncertainty acts as an important driver of risk management because national policy influences how risks are prioritised, while locally elected members determine the resources available for control of risks. Politics also limits the scope for strategic choice, as well as imposing new strategies, such as the requirement for partnership working. Both of these restrictions affect the detail of the design and day to day operation of the risk management system in the financial institutions.

2.3 Risk Management

Risk involves the likelihood and consequence of something occurring and the chance of something happening impacting on the achievement of objectives, risk management has been shown to be critical as far as organizational performance is concerned. Risk management is considered more important in the financial sector than in other business areas because the financial industry is facing a large number of risks in a volatile environment (Carey, 2001) Risk management therefore involves identifying, measuring, monitoring and controlling risks. The process is to ensure that the individual clearly understands risk management and fulfils the business strategy and objectives and thus boost the performance of the organization (Freund, 1988).

According to (Essinger and Rosen, 2006), a risk management framework encompasses the scope, the process/system/procedures to manage risks and the roles and responsibilities of the individual related to risk management and enhance the performance of the organization. The effective risk management framework includes the risk management policies and procedures that cover risk identification, acceptance, measurement, monitoring, reporting and control. (Collier and Mark 2006) reviews the risk management procedures in three parts: risk assessment, risk mitigation and evaluation and assessment. The risk assessment process includes identification, evaluation of risk impact and recommendation of risk-reducing measures. Secondly, risk mitigation involves prioritizing, maintaining and implementing the appropriate risk-reducing controls recommended by the risk assessment. Lastly, evaluation and assessment emphasize the continual evaluation process and the key factors for a successful risk management program. Organizations that implement risk management strategies are more obliged to achieve the organizational performance (Porter, 2008b), successful implementation of the risk management process involves risk identification, risk measurement and risk evaluations process.

Despite the efforts made, it is not possible to prevent or eliminate all risks due to this it is important to put in place measures to identify all risks in an organization. Finding risks can be one of the most challenging and interesting areas of risk management strategies. Detecting risk early enough helps to minimise losses and increases the likelihood of recovery for fraud that have been identified. Putting detection measures in place can also act as a deterrent, preventing potential frauds from being committed

and making the organisation more resilient to risk happening (Pearce and Robinson, 2002).

Risk measurement procedure is designed to provide the general methodology and approach to conducting a risk assessment. This includes the preparation work, risk workshop and reporting requirements. The purpose of the risk measurement is to identify the potential risks and opportunities and then rank them according to priorities, identify existing and potential control measure or risk mitigations to eliminate or minimise the risk, provide a forum to gain consensus on derived outcomes of the risk mitigations process (Normann and Ramirez 1993).

Risk measurement is the systematic application of management policies, procedures and practices to the tasks of establishing the context, identifying, analysing, evaluating, treating, monitoring and communicating risk. Risk assessment is the process of risk identification, risk analysis, risk evaluation and control. The fundamentals of risk assessment includes a combination of the consequences of the event and the probability that it will occur risks are eliminated by using various amounts and types of treatments or strategies treatments are developed and implemented to reduce risk (Hughey and Erik1997).

The final step in risk management is the risk evaluation that should be engaging and motivating. The risk evaluation process should be assigned a leader who will take up the role of risk analysis to come up with ways of continuously improving the existing risk management plan. Financial risks should be analysed based on likelihood and consequence and then rated in a way which allows management to prioritise them and

decide whether or not they are willing to tolerate them. After identifying the methods and associated controls, treatment options can then be identified (Hughey and Mussnug1997).

Risk monitoring is therefore the continuous process of tracking and evaluating the risk management process by metric reporting, enterprise feedback on watch list items, and regular enterprise input on potential developing risks. The metrics, watch lists, and feedback system are developed and maintained as an assessment activity. The output of this process is then distributed throughout the enterprise, so that all those involved with the program are aware of the risks that affect their efforts and the system development as a whole (Covello et. al,2008)

2.4 Risk Management Strategies

According to (Hubbard and Douglas, 2009) effective risk management strategies involves a comprehensive procedure undertaken by the financial institutions to avert the effects of risk factors in the organization, there are myriad of risk management strategies that will influence on the organization performance, these includes risk control which can be achieved through avoidance or reducing the effects of risk in case of an occurrence, risk financing which involves transfers and risk retention (Hunghey and Erik, 2007).

2.4.1 Risk Control

Risk control has an objective to reduce risk to an acceptable level and/or prioritize resources based on comparative analysis. Risk control includes risk aversion, risk homeostasis, discounting procedures, decision analysis, trade off analysis, insurance

models, and repair and maintainability issues which should be effectively implemented for purpose of risk; management (Pearce and Robinson 2002). Risk control is performed within an economic framework with an objective of optimizing the allocation of available resources in support of a broader goal. Therefore it requires the definition of acceptable risk, and comparative evaluation of options and/or alternatives for decision making.

According to (Boynton and Zmud, 2004) risk control can be approached by an organization within a strategic, or a system wide or an organization wide plan. A philosophy for risk control might be constructed based on recognizing that the occurrence of a consequence inducing event is the critical factor to be considered. Once the risks have been categorized and analysed, the process of handling those risks is initiated. The prime purpose of risk handling activities is to mitigate risk. The methods for doing this are numerous and fall into four basic categories;

Risk avoidance involves removing all requirements that represent uncertainty and high risk probability or consequence. Avoidance includes trading off risk for performance or other capability, and it is a key activity during requirements analysis. Avoidance requires understanding of priorities in requirements and constraints, which will help to establish whether they are mission critical and mission enhancing. Risk control is the deliberate use of the design process to lower the risk to acceptable levels. It requires the disciplined application of the systems process and detailed knowledge of the technical area associated with the design. Control techniques are plentiful and include: Multiple concurrent designs to provide more than one design

path to a solution, alternative low risk design to minimize the risk of a design solution by using the lowest risk design option. (Byars, 2001)

Risk control involves incremental development, such as pre planned product improvement, to dissociate the design from high-risk components that can be developed separately; technology maturation allows high-risk components to be developed separately while the basic development uses a less risky and lower performance temporary substitute. Test, analyse and fix that allows understanding to lead to lower risk design changes. Test can be replaced by demonstration, inspection, early prototyping, reviews, metric tracking, experimentation, models and mock-ups, simulation, or any other input or set of inputs that gives a better understanding of the risk, robust design that produces a design with substantial margin such that risk is reduced, and the open system approach that emphasizes use of generally accepted interface standards that provide proven solutions to component design problem. (Covello, et al., 2008)

2.4.2 Risk Financing

Risk financing involves a deliberate effort to manage and provide a budgetary allocation for all risks that the organization anticipates occurring, risks financing covers lows risks which do not pose more financial challenge to the organization Collier and Mark (2006). Risk financing involves risks retentions and risk transfers; Retention is the deliberate acceptance of the risk because it is low enough in probability and or consequence to be reasonably assumed without impacting the development effort. Key techniques for handling accepted risk are budget and schedule reserves for unplanned activities and continuous assessment to assure

accepted risks are maintained at acceptance level. The basic objective of risk management in organizations is to reduce all risk to an acceptable level. The strong budgetary strain and tight schedules on programs tend to reduce the organizations management capability to provide reserve. By identifying a risk as acceptable, the worst-case outcome is being declared acceptable. Accordingly, the level of risk considered acceptable should be chosen very carefully in the acquisition program (Crockford, 2006)

The transfer can be used to reduce risk by moving the risk from one area of design to another where a design solution is less risky (Crockford, 2006). Examples of this include; assignment to hardware versus software or vice versa; and Use of functional partitioning to allocate performance based on risk factors. Transfer is most associated with the act of assigning, delegating, or paying someone to assume the risk. To some extent transfer always occurs when contracting or tasking another activity. The contract or tasking document sets up agreements that can transfer risk from the government to contractor, program office to agency, and vice versa. Typical methods include insurance, warranties, and incentive clauses. Risk is never truly transferred. If the risk isn't mitigated by the delegated activity it still affects the normal functioning of the organization.

Transfer is effective only to the level where the risk taker can handle it and also a consideration on how well the delegated activity solution integrates into project or program. Transfer is effective only if the method is integrated with the overall effort. For example, whether the warranty action is coordinated with operators and maintainers, consequently transfer is effective only if the transfer mechanism is valid.

For example, if the project or program has no or little control over the risk item, then transfer should be considered to delegate the risk to those most likely to be able to control it (Alibaba, et al, 2007)

2.5 Organizational Performance

Organizational performance comprises the actual output or results of an organization as measured against its intended outputs or goals and objectives. According to Richard et al. (2009) organizational performance encompasses three specific areas of firm outcomes; financial performance (profits, return on assets and return on investment), product market performance (sales, market and share); and shareholder return (total shareholder return, and economic value added) Specialists in many fields are concerned with organizational performance including strategic planners, operations, finance, legal, and organizational development (Richard, 2009). In recent years, many organizations have attempted to manage organizational performance using the balanced scorecard methodology where performance is tracked and measured in multiple dimensions such as: financial performance (such as shareholder return) customer service social responsibility corporate citizenship, community outreach employee stewardship against the possible risk hazards.

The successful implementation of the risk management strategies will influence on the performance of the organization. According to (Hambrick and Cannella, 1989) the impact of contingency factors such as top management support, business vision, and external expertise, is the indicators of the top management support that influences on the organization performance. According to (Hughey and Mussnug 1997) the top

management support is considered a critical success factors for organization performance which concurrently influence on the risk management procedures. Top management support includes a broad range of activities in an organization, including developing project procedures that include the initiation stage, training programs, establishing a project management office, support quality management etc. (Young and Jordan, 2008) suggest that the essence of top management support related to effective decision-making to manage risk and to authorize business process change which contributes much to the organization performance.

Management improves the decision making process in order to manage risk. Top-level management responds to business processes and manages risk. Successful mitigation or bearing of risk is contingent upon commitment and support from top management which simultaneously contributes to the organizations success. Organizational performance is directly influenced by the communication channels which are important in influencing risk management strategies employed by the organization. Senior management discuss future plans with staff, internal communication therefore support business strategy and improve business processes as well as performance (Crockford, 2006).

For effective organization performance, communication is an important consideration for effective risk management. (Grabowski and Roberts, 2009) asserts that communication plays an important role in risk mitigation concurrently having a direct impact on the performance of the organization. It provides opportunities for clarification, for making sense of the organization's progress, and for members to discuss how to improve the organization and the impact of using different risk

mitigation strategies which eventually leads to organizational performance and effectiveness. Risk management is primarily associated with the fluidity of organizational structures (Boynton and Zmud, 2004).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter outlines the methods that were used in obtaining information for the study. The chapter covers the research design and explains the research instruments that were used in the study, the type and source of data and how the data was analyzed.

3.2 Research Design

This study was a case study. According to (Yin and Robert, 2002); a case study is an empirical inquiry that investigates a contemporary phenomenon within its real-life context, especially when boundaries between phenomenon and context are not clearly evident (exploratory studies). Case study research can be positivist (quantitative), interpretive, or critical, depending upon the underlying philosophical assumptions of the researcher.

Since the main purpose of the study was to establish the risk management strategies used to enhance performance by getting in-depth information from the respective respondents rather than broad and general information.(Yin and Robert, 2002)

3.3 Data Collection

The study relied mostly on primary data sources. Primary data was collected using an interview guide; this was adopted since it helps the researcher to ask Questions systematically. These were administered to five managers at the head office of the

Equity bank Ltd picked from the corporate strategy and planning, finance department, risk management, internal audit and business growth and development department, The respondents (managers) were targeted since they were in a position to provide reliable information that the study sought while Nairobi was selected due to its accessibility..

3.4 Data Analysis

The data collected from the respondents was qualitative in nature. The researcher used content analysis to analyse the data through describing phenomena, classifying it and seeing how the concepts interconnect as will be indicated by the respondents. This approach of analysis was preferred because it gives a result that is predictable, directed, or comprehensive. Content analysis also enabled the researcher to shift through large volumes of data with relative ease in a systematic fashion, Collier & Mark, S. (2006).

CHAPTER FOUR

DATA ANALYSIS FINDINGS AND DISCUSSION

4.1 Introduction

This chapter presents the analysis and interpretations of the data from the field. It presents analysis and findings of the study as set out in the research methodology on Risk management strategies used by the Equity Bank Ltd to enhance performance. The data was gathered exclusively using an interview guide as the research instrument. The interview guide was designed in line with the objectives of the study. To enhance quality of data obtained, unstructured questions were used whereby respondents gave information on risk management strategies used by the Equity Bank Ltd to enhance performance.

4.2 Response Rate

The researcher targeted 5 interviewees; however out of the 5 respondents targeted 4 completed the interview guide making a response rate of 80%. This complied with Mugenda and Mugenda (2003) who suggested that for generalization a response rate of 50% is adequate for analysis and reporting, 60% is good and a response rate of 70% and over is excellent. This commendable response rate was made a reality after the researcher made visits to request the respondent to participate in the study.

4.3 Profile of the Respondents

The study sought to document the level of the education of the respondents. This was to determine the capacity of employee to understand risk management strategies that

the organization employs in order to enhance performance. From the findings majority had attained masters, followed by those who had bachelor degrees as their academic qualification. This reveals that most of the managers at Equity bank have capacity to understand strategies that promote bank performance.

On the respondents' designation in the organization, the four Managers who responded were holding the positions of senior manager, investment manager, finance manager and business development manager. This implies that the study was able to reach the target respondent in terms of position they held in the organization and that the result can be reliable as they were conversant with the strategies of risk management that the organization applies to enhance performance.

The study, in an effort to establish the interviewees' competence and conversance with matters regarding Equity bank, sought to know the years that the interviewees had worked for the Bank. According to the interviewees' response, all of them had worked for the organization for at an average of four years as most promotions are internal, within the organization. Those who had worked for short duration had 3 years while those who had served for longer duration had 8 years, the findings revealed that most of them had stayed in the organization long enough and therefore had better understanding of the organization risk management strategies.

4.4 Risk Faced by Equity Bank

The study requested the interviewees to indicate the main risk that the bank has been prone to, from the study findings a numbers of risks were shown to affect Equity bank. The Bank's business units have identified a range of possible risks which have

been mapped indicating risk drivers, frequency, impact, risk levels, trends, risk owners and the respective mitigating strategies. The Bank has already established a Risk Management Department to ensure compliance with the Bank's risk limits. All risks associated with banking institutions and those that are specific to Equity Bank, are actively managed by the respective business units and monitored by the Risk Management Department. The Bank's risk limits are assessed regularly to ensure the appropriateness in line with the Bank's objectives and strategies and current market conditions.

Some of the risks that were pointed out by the respondents include inflation risks which are the risks associated with uncertainty of the future value of an investment due to inflation, Liquidity risk which is the risk that a bank may not be able to meet its short term financial demand. Equity bank also faces Credit risk which is a risk that a borrower will default on any type of debt failing to make required payments. Another risk faced by the bank is political risk which is the risk of financial, market or personnel losses due to political decisions or disruptions. Currency risk is also another risk face by Equity bank which arises from the change in price of one currency against another. All these risks are managed by Equity bank through mitigation strategy of Risk control and Risk financing.

4.5 Risk management Strategies used by the Equity Bank

On the risk Management strategies that have been adopted by the banks, most of the respondents highlighted the following mitigation strategies;

4.5.1 Risk Control

This strategy includes trading off risk for performance or other capability, and it is a key activity during requirements analysis. Most of the interviewees reported that avoidance requires understanding of priorities in requirements and constraints, which will help to establish whether they are mission critical and mission enhancing. Further they reported that this includes not performing an activity that could carry risk.

Inflation risks

Inflation risk is the uncertainty over the future real value (after inflation) of an investment. The findings revealed that equity bank has faced inflation risks as noted by the respondents where Inflation portends a business risk to the extent that the business is unable to pass cost increases to customers. This is considered to be a significant risk because the Bank's current and forecast operating margins cannot absorb moderate inflationary cost increases while maintaining a competitive return on investment. The Bank therefore factors prudent allowance for inflation into its financial forecasts. Equity bank's pricing strategy takes into account the market inflation tendencies which are laid out in bank's contractual documents and tariffs. Market intelligence and research is also conducted to check on the inflation trends to help mitigate such risks.

Credit risks

The Bank's credit risk is primarily attributable to its loans and advances. The Bank structures the level of credit risk it undertakes by placing limits on amounts of risk accepted in relation to one borrower or a group of borrowers. Such risks are

monitored on a regular basis and are subject to monthly or more frequent review. Exposure to credit risk is managed through analysis of the ability of borrowers and potential borrowers to meet interest and principal repayment obligations, obtaining collateral and corporate guarantees where considered necessary and the Bank has a Debt Recovery Unit which is in charge of follow-up and collections.

Liquidity Risk

Liquidity risk arises in the general funding of the Bank's activities and in the management of positions. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame. The Bank has access to a diverse funding base. Funds are raised mainly from deposits and share capital. The Bank continually assesses the liquidity risk by identifying and monitoring changes in funding required to meet business goals and targets set in terms of the overall Bank strategy.

Political risks

Respondents reported that Political Risk is the likelihood of loss of business due to political upheavals and civil strife, expropriation of assets by the state, as well as adverse changes in Government policies. At present, Equity Bank conducts all its business in Kenya. Kenya has a long history of political stability in a turbulent region, consolidated over the last decade during which the country has made a peaceful successful transition from one party state to multiparty democracy. With regard to political risk, the Government's stated policy is to create an enabling environment for private sector led development. However guarantees or insurance cover losses caused

by specified political risk events are typically termed partial risk guarantees or Political Risk Guarantees or political risk insurance depending on the provider. Partial risk guarantees cover commercial lenders in private projects. These typically cover the full amount of debt. Payment is made only if the debt default is caused by risks specified under the guarantee. Such risks are political in nature and are defined on a case-by-case basis. Therefore the Bank is apolitical; it has a national outlook and complies with all regulatory requirements to reduce such political risk.

Currency risk

The Bank has very little exposure in foreign currency through transactions in foreign currencies, as this is a new area that the Bank ventured into after conversion to a commercial bank. The Bank has however engaged an experienced management team to handle both foreign exchange and trade finance. The bank's exposure is limited to 20% of the core capital.

4.5.2 Risk financing

The financial impacts of disasters have been mitigated by the equity bank through proactive financial management tools, most notably risk financing and risk transfer tools and compensation arrangements provided have been provided by the equity bank as a complement to physical risk reduction measures. These tools provide financial protection and reduce costs by reprofiling risks across time so that they can be better managed or by transferring risks to those better to able to absorb them. They reduce financial vulnerability, thus averting potentially devastating drops in welfare

and ensuring that resources are available for rapid response, recovery and reconstruction, including important post disaster investments in risk reduction.

The development of effective risk financing and risk transfer strategies by equity bank requires a good understanding of risk exposures within the economy and risk-bearing capacities, which taken together reveal financial vulnerability. Financial vulnerability reflects the extent to which a financing gap might emerge as a result of a disaster, causing financial hardship or distress which equity bank has taken initiative to avert; as a measure of financial capacity, it provides a reference point for assessing the costs and benefits of financial tools and elaborating financial planning more broadly. Other risks that could be mitigated through risk financing are rapid expansion risk where the Bank has been building capacity, in both training and recruitment of professional and qualified staff, acquisition of a robust IT system that may comfortably handle 10,000 transactions per minute and enhancing its corporate governance structures. While some may be able to cope with the financial impacts of disasters without having recourse to financial tools, others may clearly benefit from such tools despite their costs.

Risk financing and risk transfer strategies interact with physical risk reduction. In order to enable the functioning of risk financing and transfer markets, disaster risks must not only be properly assessed, but also reduced to levels that allow for cost effective risk financing or risk transfer. In this regard, these markets, where they exist, may highlight critical risk reduction measures requiring governmental investment. They may also increase risk awareness and incentivise individual risk reduction measures where such opportunities exist through risk-based pricing or by means of adjustable loss sharing mechanisms such as deductibles and co-insurance. A positive

feedback loop in risk reduction has thus been created with risk financing and risk transfer markets.

4.5.3 Successful implementation of risk management strategies

Further the interviewer sought to ascertain from the respondents on the extent that their bank has successfully implemented the risk management strategies, majority of the respondents reported that Equity bank has successfully implemented the strategies to manage threats uncertainties with negative consequences, typically including transferring the threat to another party, avoiding the threat, reducing the negative effect or probability of the threat, or even accepting some or all of the potential or actual consequences of a particular threat, and the opposites for opportunities uncertain future states with benefits, further the interviewees contended that certain aspects of many of the risk management standards have come under criticism for having no measurable improvement on risk, whether the confidence in estimates and decisions seem to increase, but this notwithstanding the bank has made tremendous progress to implement the risk management strategies successfully.

4.6 Effects of risk Management strategies on performance

Risk management strategies have had tremendous effects on the performance of Equity bank through performance indicators.

4.6.1 Indicators on Equity bank performance

The study requested the respondents to mention some of the indicators on the bank performance, most of the respondents mentioned increase in customers accessing the products of the bank as key indicator of the bank performance. Other respondents

indicated that as a result of performance, equity bank enhanced their customer-profitability calculation and analysis capabilities. Capturing accurate and comprehensive data on customers' overall relationships with the bank in terms of accounts, products and sales and service interaction has been a major focus on the indicator of the bank performance. Other respondents reported that performance of equity bank can be measured by assessing which customers or groups of customers are profitable or unprofitable and why, provides equity bank with information upon which to make marketing and pricing decisions which are key indicators of the bank performance.

4.6.2 Risk management and Bank performance

On whether the implementation of the risk management strategies contributed to the performance of the bank, the interviewees unanimously agreed that the implementation of the risk management strategies contributed to the performance of the bank, other respondents mentioned the progress in the growth of client base, increased annual profit returns as some of direct indicators on the performance of equity bank which has been realized as a result of the implementation of strategies.

Some of the interviewees reported that there was tremendous growth on the sub branches which could be justified by the increase in the number of banked branches which were being opened countrywide, further they maintained that the number of clients opening accounts with the new branches has been increasing considerably, these were clear indicators of growth in these branches. Further majority of the interviewees reported that the bank has in the recent past introduced other products in the markets such as agent banking and mobile banking services by penetrating into the market which has since been received positively by the clients, the interviewees

maintained these were clear indicators that the risk management strategies led to such performance.

4.6.3 Recommendations on other strategies related to performance

On what the bank can do to improve on the risk management strategies, most of the interviewees recommended that the bank should adopt integration approach where they integrate human-resources systems into the strategic plan, moreover the respondents reported that the bank should identify, assess, plan and implement the risk management strategies, more so the respondents reported that the bank should keep records on the risk retention strategies so as to be able to follow track of all the risks, also effective reporting procedure on the risk occurrence should be considered effectively.

4.7 Discussion of the findings

Equity bank suffer from a number of risks which includes inflation, liquidity, currency, credit and other geopolitical risks that are present in bank which pose new oversight for Equity bank. The findings under this section therefore conform to the literature reviewed as according to (Covello, et al., 2008) confirms that financial institutions are prone to vast of risks, for this case Equity bank has faced a number of risks as discussed.

Equity bank has adopted a number of risk management strategies such as risk Avoidance which includes trading off risk for performance or other capability, and it is a key activity during requirements analysis. Avoidance requires understanding of

priorities in requirements and constraints, which helps to establish whether they are mission critical and mission enhancing. According to these revelations inflation risk has raised reserves requirement which is the amount the bank must keep in hand at the end of each day. Furthermore credit risks is the risk that a borrower will default on any type of debt by failing to make the required payment, thus equity bank performs a credit check on the prospective borrower to take out appropriate insurance such as mortgage insurance or seek security or guarantees of the third party, this will help the bank in financial risk mitigation by acknowledging the customer's credit worthiness before carrying out any further transaction, the findings therefore implies that equity bank has adopted a number of strategies towards risk mitigation process. The study revelation therefore conform to the literature reviewed as according to (collier and Mark 2006) alludes that various risk strategies are available for the exploitation by the bank

Equity bank has adequate capital which enables them to contain and manage risks through, fixed exchange rates, stable interest rates, capital controls, and oligopolistic banking markets which enhance profitability from low risk business, thus ability to overcome the effects of the equity risks. Equity risk is often referred to in the bank through the purchase of stocks, and does not commonly refer to the risk in paying into real estate or building equity in properties. The findings revealed that measure of risk used in the equity markets is typically the standard deviation of a security's price over a number of periods. The standard deviations thus delineate the normal fluctuations bank can expect in that particular security above and below the mean, or average, the findings therefore implies that strategies adopted by equity bank have enabled it to adequately control its risks which has enhanced its performance, the study findings conform to the literature reviewed in the study as according to (porter, 2008b) who

alludes that fixed exchange rates, stable interest rates, capital controls and oligopolistic banking markets are proper indicators of risk control mechanisms.

Central banks have a key role in developing local debt markets. The development of local currency bond markets is critical to equity bank financial development and resilience to shocks. Furthermore government fiscal and debt management policies should not undermine effective monetary policy since good macroeconomic policy requires mechanisms that ensure appropriate coordination but avoid potential conflicts of interest, thus enhancing the financial system stability of the bank. Consequently on political risks, Equity bank uses the new accord to focus bank wide attention on efforts to achieve risk-management leadership. The findings revealed that Basel II has been good news for banks whose risk-management efforts has begun with the best of intentions and have languished through inattention, the revelations therefore implies that the development of local currency bond markets is critical to the equity bank management, the findings conforms to the literature reviewed (Pearce and Robinson, 2002) which play a key role in developing local debt market.

Equity bank has used Open market operations, the discount rate and reserve requirement to control the risks associated with the inflations, using these three tools, the reserve influences the supply and demand for reserve balances of commercial banks at the central bank, and in this way alters the funds rate which is the interest rate at which banks lend their excess reserve balances to other banks that have reserves below the system's requirements. Further the study revealed that open market operation is an activity by a central bank to buy or sell government bonds on the open market. A central bank uses them as the primary means of implementing monetary policy. This has helped the equity bank to manipulate the short term interest rate and

the supply of base money in an economy thus indirectly controlling the total money supply, in effect expanding money or contracting the money supply. This also involves meeting the demand of base money at the target interest rate by buying and selling government securities, or other financial instruments (Normann and Ramirez 1993). On risk aversion the study revealed that during the financial crisis, the stability of the equity bank and the provision of loans to the real economy attract the particular attention of policymakers and banking supervisors. Increases in risk positions and banks' risk perception, which were triggered by the crisis, leads to a change in the behaviour of banks. A deleveraging process is thus initiated and internationally active banks accelerate the cut-back of their cross-border activities (Hughey and Erik 1997), these findings therefore imply that equity bank has employed the use of open market operations, discount rate and reserve requirement to manage its risks, the revelations also conform to the literature reviewed.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary of the data findings on the analysis of risk management strategies used by equity bank to enhance performance, the conclusions and recommendations are drawn there to. The chapter is structured into summary of findings, conclusions, recommendations and area for further research

5.2 Summary

According to the study, majority of the interviewees had attained Masters Degrees followed by those who had bachelor degrees as their academic qualification. This reveals that most of the managers at equity bank have capacity to formulate strategies that can be reliable and improve performance because they held positions such as senior manager, investment manager, executive banking and finance managers thus they gave reliable results due to their positions and had been serving for longer durations.

The study revealed that equity bank suffer from a number of risks which includes inflation risk, liquidity, currency risks, credit risks and other geopolitical risks which poses new oversight for the Equity bank. Equity bank has adopted a number of risk management strategies which includes risk control strategies which includes trading off risk for performance. Risk control requires understanding of priorities in requirements and constraints, which helps to establish whether they are mission critical and mission enhancing. The findings revealed that measure of risk used in the

equity markets is typically the standard deviation of a security's price over a number of periods. The standard deviations thus delineate the normal fluctuations bank can expect in that particular security above and below the mean, or average.

More over the findings revealed that Central bank have a key role in developing local debt markets. The development of local currency bond markets is critical to equity bank financial development and resilience to shocks. Also the government fiscal and debt management policies should not undermine effective monetary policy since good macroeconomic policy requires mechanisms that ensure appropriate coordination but avoid potential conflicts of interest, thus enhancing the financial system stability of the bank. Consequently on political risks, Equity bank uses the new accord to focus bank wide attention on efforts to achieve risk-management leadership.

5.3 Conclusion

From the study it is evident that risk management is a key aspect in determining the bank performance. Risk management enables the organization to classify its customers for better service, as close attention is given towards each and every customer to build their confidence. Risk management involves identifying the risks and taking appropriate approaches to mitigate these risks at the good of the organization as a whole and concurrently boost the confidence of the clients.

5.4 Recommendations of the Study

The study recommends that corporations should come up with effective risk management strategies which focus on the needs and wants of the customer towards building their confidence. Identified risks should be dealt with appropriately before

their effects spill over to the organization clients. Also managers should be able to identify the dynamic risks of the customer in order to keep abreast with the changing threats that are likely to impact on the performance of the bank.

5.5 Limitation of the Study

The data collection period took a longer time than was previously envisaged since it was hard to get managers to participate in the interview schedule. It took many visits to finally get the information needed hence it was time consuming and tiresome as well.

The researcher also encountered other challenges or limitations such as non-cooperation from the managers since it was not easy to convince them to give the information on the risk management strategies because they perceived ‘information as power’ and they were reluctant to disclose full information especially the risks they were facing. However, the researcher assured the respondents of proprietary measures that the findings would be accorded and used only for academic purpose.

5.6 Suggestion for Further Studies

The study suggests that further research should be undertaken on the extent of the risk management on organizational performance of Equity bank. The study also suggests that further study to be done on the effect of credit risk on performance in the banking sector in order to depict a reliable result that covers the whole sector.

5.7 Recommendation for policy and practice

The findings of this study would be beneficial to the firms participating in the banking institution market since it would point on the risk management strategies and thus will aid them in assessing the performance in the financial market. The study finding would give a guide on the requirements by the banking institutions to control fraud and other risks associated with cash.

The study also recommends to the policy regulators like Central Bank of Kenya in considering the pivotal position played by the banking institutions in the Kenyan current economy to develop policies that enhance the growth of the banking sector. Equity bank through its strategies has opened more branches improving the economy of the country therefore such performance should be recommended through policies that will boost the industry as whole.

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Appendix I: Interview Guide

SECTION A: GENERAL INFORMATION

1. Name of the respondent (optional)
2. What is your highest level of education?
3. What is your designation at Equity Bank of Kenya?
4. How long have you worked for Equity Bank of Kenya?

SECTION B: RISK MANAGEMENT STRATEGIES

5. What are some of the risks banks are prone to?
6. If your bank is prone to risks, how frequent do these risks occur in your Bank?
7. Are there risk mitigation strategies that have been adopted by your bank?
8. Explain how your bank respond to the following risks;
(Inflation risks, credit risks, refinancing risks, equity risks, financial system stability risks, political risks and legal risks)
9. How does your organization carry out risk control on inflation risks?
10. How does your bank carry out risk aversion on financial system stability risks?

11. What are some of the risk financing approaches adopted by the bank in risk control?

12. How effective are the risk management strategies in your bank?

SECTION C: EFFECTS OF RISK MANAGEMENT ON PERFORMANCE

13. What are some of the indicators on your bank performance?

14. To what extent has your bank successfully implemented risk management strategies?

15. How has the implementation of risk management contributed to the performance of your bank?

16. Has your Bank experienced growth in the number of branches due to risk management approaches?

17. To what extent has the risk management by your bank contributed in building customer trust?

18. What can the bank do to improve on risk management strategies on enhancing its effectiveness and performance?