STRATEGIC RESPONSES BY HOUSING FINANCE COMPANY OF KENYA LIMITED TO THE ENVIRONMENTAL CHALLENGES FACING THE MORTGAGE INDUSTRY IN KENYA

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OCTOBER, 2014
DECLARATION

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

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

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To my wonderful family for your constant encouragement and support, and to my friends for being such great cheerleaders.
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ABSTRACT

The mortgage industry in Kenya faces a challenging environment. The study sought to determine the environmental challenges facing the mortgage industry in Kenya, and strategic responses adopted by Housing Finance Company of Kenya Limited to such challenges. The study revealed that industry faces high costs all around. From the cost of land, to cost of building and construction, to interest rates, taxation, as well as the challenge of providing long term funding using short term funds. These high costs increase the costs of mortgages, causing mortgages to be out of reach for the majority of Kenyans. Many people are also afraid of taking up mortgages, due to the fear of consequences if they are unable to pay, causing them to seek for personal loans instead. From the research, it emerged that political factors also pose a big challenge to the industry. Government does not have a clear focus on the housing industry, and most of the solutions to the issues facing the industry lie with it. The research design applied in the study was a case study. The primary data was collected using interview guide administered to four interviewees who are part of the top management team. The analysis of the qualitative data gathered was done using content analysis. The study unearthed strategic responses by Housing Finance Company of Kenya Limited. Product innovation has been a major factor for the company, by addressing the affordability issue. Through flexible products that enable customers to save and offering a higher percentage of the loan amount, more people are able to afford mortgages. Restructuring along the real estate value chain has also enabled the organization to focus on different areas of the industry, including development, property sales and insurance. It has also diversified its offering to create new funding sources by going into full scale banking. To solve the funding issue, it has so far issued two corporate bonds, which have helped ease the funding gap. With the realization that the government holds the keys to changes for the industry, the organization engages in lobbying directly and through bodies like Kenya Private Developers Association and Kenya Private Sector Alliance to push for policy and legislative changes that will be favourable for the industry. It is also working on its IT systems to integrate the new structure to ensure efficiency and rejuvenating the internal culture to reflect the new status of the company. Housing Finance set up the Housing Finance Foundation, to help the industry in training and nurturing talent for the building and construction industry, which is not well trained. The organization is therefore positioning itself as more than just a mortgage company, but as an integrated solutions enabler for the property industry. The research concludes that Housing Finance has effectively responded to environmental pressures, through strategic planning and management. However, the researcher concludes that there is need to carefully approach the focus on the real estate value chain. There is a risk of the company trying to do too much which is potentially detrimental to the business in provision of expertise and competitiveness. The researcher therefore concludes that company should think about outsourcing needs such as construction and technology rather than creating its own capabilities. Creating more strategic alliances and joint ventures on projects will allow it to focus on its area of expertise and build capacity for better competitiveness.
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ABBREVIATIONS AND ACCRONYMS

BAICL: British American Investments Company Limited
CBK: Central Bank of Kenya
CDC: Commonwealth Development Corporation
CRB: Credit Referencing Bureau
GDP: Gross Domestic Product
CMA: Capital Markets Authority
HF: Housing Finance Company of Kenya Limited
KCB: Kenya Commercial Bank
KBS: Kenya Building Society
KRA: Kenya Revenue Authority
NSSF: National Social Security Fund
REITS: Real Estate Investment Trusts
S&L: Savings and Loan
SACCO: Savings and Credit Cooperative Organization
CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Organizations exist as open systems and hence they are in continuous interaction with the environment in which they operate. The environment in which the organizations operate is never static. All organizations lend themselves to this environment, which is highly dynamic, chaotic, and turbulent that it is not possible to predict what will happen and/or when it will happen. Consequently, the ever-changing environment continually presents opportunities and challenges. To ensure survival and success, firms need to develop capability to manage threats and exploit emerging opportunities promptly. This requires formulation of strategies that constantly match capabilities to environmental requirements. Success therefore calls for proactive approach to business (Pearce and Robinson, 2003).

Environmental influence has not spared the mortgage industry in Kenya. The mortgage industry in Kenya is quite undeveloped, with only one core mortgage lender, and lack of a viable market in the rural areas. Among other factors, high interest rates and high costs of construction have limited the reach of mortgages to majority, with only 2.5% of Kenyans being able to afford mortgages. Housing Finance Company of Kenya Limited (Housing Finance) has been in the mortgage industry for 49 years, and has instituted various strategic responses to cope with the challenges it faces from the environment.

1.1.1 Concept of Strategy

According to Porter (1991), strategy refers to top management’s plans to develop and sustain competitive advantage; a state whereby a firm’s successful strategies cannot be easily duplicated by its competitors so that the organization’s mission is fulfilled. Strategy
is the creation of a unique and valuable position, involving a different set of activities. If there were only one ideal position, there would be no need for strategy. The essence of strategic positioning is choosing to perform activities differently or to perform different activities than rivals. Strategy is the direction and scope of an organization over the long term, which achieves advantage in a changing environment through its configuration of resources and competences with the aim of fulfilling stakeholder expectations (Johnson and Scholes, 2002).

Many organizations develop strategies at three different levels. These three different and distinct levels of strategy are corporate, business, and functional: Corporate-level strategy is developed by top-level management and the board of directors. The corporate-level strategy seeks to determine what businesses a corporation should be in or wants to be in. These strategies address how the strategies of those businesses will be coordinated to strengthen the organization's competitive position and how resources will be allocated among businesses. Business-level strategy concentrates on the best means of competing within a particular business while also supporting the corporate-level strategy. Functional-level strategy focuses on action plans for managing a particular functional area within a business in a way that supports the business-level strategy. Functional areas include operations, marketing, finance, human resource management, accounting, research and development, and engineering. Coordinating strategies across these three levels is critical in maximizing strategic impact (Hill, Jones and Schilling, 2013).

1.1.2 Environmental Challenges

All businesses operate as open systems. They constantly interact with their external environment. Response strategies to this environment can be operational, strategic, and corporate or business oriented. Johnson and Scholes (2002), argue that strategic responses
are mainly concerned with decisions and actions meant to achieve business objectives. Operational strategies are concerned with how the component part of an organization delivers effectively the corporate and business level strategies in terms of resources, processes and people (Johnson and Scholes, 2006).

The operating environment, also called the competitive or task environment, comprises factors in the competitive situation that affect a firm’s success in acquiring the needed resources or in profitably marketing its goods and services. Among the most important of these factors are the firm’s competitive position, the composition of its customers, its reputation amongst suppliers and creditors, and its ability to attract capable employees. The operating environment is typically much more subject to the firm’s influence or control than the remote environment. Thus the firm can be more proactive (as opposed to reactive) in dealing with the operating environment than in dealing with the remote environment (Pearce et al, 2007).

Political factors refer to government policy. Political decisions can impact on many vital areas for business such as infrastructure, health and education of the work force. Pearce and Robinson (2005), reckon that the direction and stability of political factors are a major consideration for managers on formulating organizational strategy. The political environment includes elections, legislation, government structure, consumer protection, wars and conflicts. Political instability in the country owing to constitution referendum, elections and general political activity has caused many would-be investors to adopt a wait and see attitude.

Economic factors concern the nature and direction of the economy in which a firm operates and include the domestic economic situation, overseas economies and economic
trends relevant to an organization. The economic conditions affect how easy or hard it is for a firm to be successful and profitable at any time. A firm must therefore include these factors in its strategy formulation (Pearce and Robinson, 2005). The Kenyan market has faced challenging economic times that have impacted negatively on the mortgage industry. The prevailing high interest rates are as a result of a stringent monetary policy being pursued by the Central Bank of Kenya in an effort to fight high inflation have dampened the market. Land prices in the country are continually rising. Land is the most important input in for the mortgage industry, and as land prices increase, mortgage costs rise, adding pressure to an already unaffordable product. The costs of building and infrastructure in putting up housing is also very high, further pushing up mortgage prices.

The social factors that affect an organization involves the beliefs, values, attitudes, opinions and lifestyles of persons in the firms external environment, as developed from cultural, ecological, demographic, religious, educational and ethnic conditioning (Pearce and Robinson, 2005). For managers, informed judgment of the impact of changes in social cultural factors is paramount. A social analysis includes demographics, lifestyle changes, population shifts, education, living standards, earning capacity, increased social awareness and media views.

Pearce and Robinson (2005) observed that a technological breakthrough can have a sudden and dramatic effect on an organization’s environment. Technology can therefore reduce costs, improve quality and lead to innovation. The rapid changes in technology mean a rapid increase in new inventions, obsolescence of existing technologies, competing technological developments, technology legislation and innovation potential. Mobile money transfer services have resulted in greater efficiency for both financial companies and customers, and reduced cost of operation.
Pearce and Robinson (2005), define ecology as the relationship between human beings and other living things and the air, soil and water that support them. Organizations are increasingly being called upon to pay attention to this by protecting the environment. With major climate changes occurring due to global warming and with greater environmental awareness, this external factor is becoming a significant issue for organizations.

Legal factors are related to legal litigious aspects that organizations operate in. In recent years there have been many significant legal changes that have affected organizations behaviour. Legal changes can affect an organization’s costs and also alter demand (Pearce and Robinson, 2005). Legislation that has affected companies in the financial services sector includes base capital requirements by the Central Bank of Kenya as well as board composition requirement by the Capital Markets Authority. This has caused banks, insurance companies and brokerage firms to source for funding or merge.

1.1.3 Strategic Responses
Chandler (1962) stated that strategy determines the basic long-term goals of an enterprise, and the adoption of courses of action (strategy as plan of action) and the allocation of resources necessary for carrying out these goals (strategy as resource allocation). While Porter (1996) viewed strategy as the process of creating a unique and valuable position with means of a set of activities in a way that creates synergistic pursuit of the objectives of a firm.

Mintzberg (1994) defines strategy as a plan, a pattern, perspective and position. As a plan because strategy defines the means through which an organization moves from one state
to another, that is from bad to good state. Strategy is also defined as a pattern since it is concerned with repetitive actions over a period of time. Further, he defines strategy as a perspective since it provides a clear vision and a sense of direction of where the organization is heading. Finally he defines strategy as a position, which means that organizations are willing to offer particular products and services to new markets other than the existing markets. This therefore implies that they are able to position themselves better in new markets by offering new products or services.

Firms respond in a number of ways to the challenges they face from the external environment. Differentiation is an approach under which an organization aims to develop and market unique products for different customer segments. Since the product is unique, this strategy provides high customer loyalty (Porter, 1991). In a differentiation strategy a firm seeks to be unique in its industry along some dimensions that are widely valued by buyers. It selects one or more attributes that many buyers in an industry perceive as important, and uniquely positions itself to meet those needs. It is rewarded for its uniqueness with a premium price.

Firms also respond using focus strategies. According to Hill and Jones (2001), focus strategy concentrates on serving particular market niche, which can be defined geographically, by type of customer or by product line segment. It is directed towards serving the needs of a limited customer group or segment. Cost leadership is where a firm sets out to become the low cost producer in its industry. The sources of cost advantage are varied and depend on the structure of the industry. They may include the pursuit of economies of scale, proprietary technology, preferential access to raw materials and other factors. A low cost producer must find and exploit all sources of cost advantage. If a firm
can achieve and sustain overall cost leadership, then it will be an above average performer in its industry, provided it can command prices at or near the industry average. Diversification is another response strategy, and is the process of entering new business markets with new products. Such efforts may be undertaken either through acquisitions or through extension of the company’s existing capabilities and resources. It seeks to increase profitability through increased sales volumes obtained from new products and new markets. Diversification can occur at the business unit level through expansion into a new segment of an industry, in an industry in which the business is already in, or at the corporate level by entering a promising business outside of the scope of the existing business (Hill and Jones, 2001).

Strategic alliances are applied in response to economic and competition challenges. A strategic alliance is an agreement between two or more parties to pursue a set of agreed upon objectives needed while remaining independent organizations. This form of cooperation lies between mergers and acquisitions and organic growth. (Hill and Jones, 2001). Restructuring is another response to challenges in the environment. Jensen and Meckling (1976), argue that a company is a collection of contractual relationships among various stakeholders, including shareholders, suppliers, employees and customers. Restructuring is the process by which firms change these relationships. On an operational level, organizations in the financial services sector adopt responses such as product offering diversification, new product design to enhance affordability, branch and regional expansion, relationship marketing, financing, customer-care focus, innovation and information technology in order to respond to challenges in the industry.
1.1.4 The Mortgage Industry in Kenya

Kenya’s mortgage market is the third most developed in Sub-Saharan Africa, with mortgage assets equivalent to 2.5% of Kenya’s GDP. Only Namibia and South Africa rank higher. Mortgage Finance Institutions, like Commercial Banks, are licensed and regulated pursuant to the provisions of the Banking Act and the regulations and Prudential Guidelines issued thereunder. There are 45 licensed commercial banks and one mortgage finance company. Currently, mortgages are offered mainly by commercial banks and the single mortgage finance company, but Microfinance Institutions and SACCO’s have also taken also offering housing micro finance.

The focus on the mortgage industry is clear. Mortgage products are widespread and are offered by most banks. KCB acquired Savings & Loan (S&L) to specialize in mortgage finance. It has branches dedicated to mortgage finance customers through this wholly owned subsidiary. Co-operative Bank has created the Good Home Mortgage solution for the specific needs of Co-operative Societies and Unions. The main aim of the product is to assist those co-operatives that have an interest in either developing housing projects, or wish to support their members own a home. Other major banks such as Barclays, Standard Chartered and CFC Stanbic also provide a high percentage of the mortgage lending in Kenya. Overall Housing Finance Company of Kenya Limited and KCB’s S&L control over half the market and only 9 banks (6 large, 2 medium and 1 small bank) have a mortgage portfolio exceeding Kshs 1 billion.

The mortgage market in Kenya is quite undeveloped, with only one core mortgage lender in the country. In 2011, the Central Bank interest rate increased sharply, causing interest rates in the market to move from an average of 14% to 24%, leaving many mortgage takers in distress after their mortgage payments doubled. However, this rate dropped in
2012, but despite the rate stabilizing at 9.5%, which would result in a 4% spread, meaning rates lending rates of between 13 to 14%, the average lending rate is still next to 18%. This has caused mortgage facilities to remain out of reach for the majority of Kenyans. Long term and sustainable solutions to funding of mortgages are required to solve this challenge.

A typical mortgage loan would be done at variable rates for around 14% for an amount of Kshs 4 million over a period of 15 years. Based on this, 2.4% of the total population could afford a mortgage for a basic house. This rises to 11% of the urban population. There is no viable market in rural areas given the low levels of income together with the high costs of developing a distribution network. The potential size of the mortgage market is currently around Kshs 800 billion or $9.9 billion around 13 times the current level. A greater proportion of the new housing stock that came to market in 2011 was reachable by mortgaged buyers than in any previous year, at 38% of new builds, compared with 34% in 2010. The mortgage market has also increased from 7,600 homes in 2006 to 20,000 homes in 2012 but the recent hikes in interest rates have slowed down mortgage uptake.

The Kenyan mortgage industry has, in the recent past, seen the introduction of innovative products to enable growth of the industry. Such products include fixed rate mortgages that are available for 10 to 15 years, 100% financing for the full value of a house, as well as mortgage insurance against the risk of loss of income by a borrower. Other moves, such as Retirement Benefits Authority allowing pension contributors to use up to 60% of their contribution to secure mortgages is a great innovation that can leverage assets worth up to Kshs. 290 billion and increase access for lower earning individuals who have accumulated substantial pensions.
1.1.5 Housing Finance Company of Kenya Limited

The company was incorporated on 8th November 1965 as per the Banking Act. Today, the company controls over 35% of the mortgage market in Kenya. The founding shareholders were the Commonwealth Development Corporation, with 60% shareholding and the Government of Kenya with 40% shareholding. The Government of Kenya increased its shareholding to 50% in 1970. In 1984, the company completed phase five of Buru Buru estate, with a total of 4,789 units.

In 1992, the company offered part of its equity to the public and became a quoted company on the Nairobi Stock Exchange, with 39.2% offered to Kenyan institutional and individual investors, and CDC and the Government of Kenya each retaining 30.4%. Shareholding recently stood at 3.66% Government, 24.85% Equity Bank Ltd, 12.37% Equity Nominees Ltd, 8.86% BAICL, 6.82% NSSF and 43.44% to the public. Equity Bank, however, recently made a decision to sell its stake to BAICL.

In 2001, Housing Finance Company of Kenya Limited completed phase four of Komarock estate, with a total of 4,412 units built. The year 2002 signaled a significant change for the organization when the company re-branded. Out of Housing Finance Company of Kenya Limited was born the vibrant and aptly named Housing Finance. A company built on the strength of the old; yet clearly focused on availing new housing opportunities to homeowners, and meeting the growing housing challenges of today. In 2010 the company successfully raised Kshs. 7 Billion against a target of Kshs. 5 billion by way of a bond. In 2012 the company raised another 5.2 billion against a target of 2.9 billion. The company has three subsidiaries: It revived its property development arm Kenya Building Society in 2012, which has embarked on construction of Komarock
estate phase 5A. It also created the Housing Finance Insurance Agency and its social investment arm Housing Finance Foundation, whose main agenda is to create an army of one million artisans by 2016 to supply skilled labor to the region and beyond.

1.2 Research Problem

In a broad sense, the environment is infinite and includes everything outside the organization. Thus organizational environment refers to all elements that exist outside the boundary of an organization and have the potential to affect all or part of the organization. Response strategies refer to the actions taken by an organization reacting to changes in the environment, to determine the direction and scope of an organization over the long-term. The aim of these responses is to achieve advantage for the organization through its configuration of resources to meet the needs of markets and fulfil stakeholder expectations (Johnson and Scholes, 2002).

This study set to find out how Housing Finance has responded to environmental challenges posed by the environment. The company has been successful despite a number of challenges it faces, which include the High Central Bank Rate that has remained at 8.5%, the high inflation rate and the high cost of building material. Despite the growing middle class, the number of Kenyans who can afford qualify for mortgage facility is below 2.4% in Kenya, and 11% of the urban population. This research was to study the various challenges faced by Housing Finance and the responses that the company has instituted.

Several studies have attempted to analyze the strategic responses of firms in the financial services sector to various challenges facing them. These include Kipyator (2011), who investigated strategic responses by National Bank of Kenya to the environmental
challenges within the financial sector in Kenya, and Manani (2013) who studied strategic responses by Kenya Commercial Banks to Environmental Challenges. While these studies focussed on the financial services sector, none narrowed in on the mortgage industry, despite mortgage financing being offered by most banks. Nkirote (2004) investigated environmental challenges and strategic responses in the mortgage industry in Kenya. There have been significant changes in the mortgage and financial sector in Kenya since then, and study focused on Housing Finance Company of Kenya Limited and took into account the various changes that have taken place in industry and market since then.

Being the single mortgage finance institution in the country, Housing Finance needs to ensure it positions itself in a manner to enable it respond to the challenges facing the mortgage industry in order to grow its market share. It is against this background that this study of the strategic responses adopted by Housing Finance to the challenges facing the mortgage industry comes. This research used case study approach, to answer the following questions; what are the environmental challenges facing the mortgage industry in Kenya? how has Housing Finance responded to these environmental challenges?

1.3 Research Objectives

The objectives of the study were:

i. To determine the environmental challenges facing the mortgage industry in Kenya

ii. To determine the strategic responses adopted by Housing Finance Company of Kenya Limited to such environmental challenges
1.4 Value of the Study

Companies that offer mortgage facilities will find the study useful in responding to the various challenges facing the industry. The limited reach of the mortgage market is clear and there is still a need to look at other forms of improving access to financing for housing among lower income groups. This study provides an analysis of how mortgage providers could respond to these challenges as well as how lenders can manage the risks from mortgage lending.

Policy makers such as the Central Bank of Kenya will be able to use the findings of this study to have a better understanding of the challenges facing mortgage facility providers in Kenya, enabling them to set policies that will strengthen the industry. The CBK will be able to consider exploring more prescriptive rules which would set some minimum product standards for mortgage loans in terms of both loan to value and payment to income with a view to ensuring ‘responsible’ lending for the protection of both consumer and lender, and also learn the current level of provision of financial services and Housing Finance to lower income groups and what capacity improvements are required.

The study will also provide a knowledge resource for future managers at Housing Finance, by providing a perspective on the reasons behind corporate, functional and unit strategy decisions made at the company. It will enable them to seek out further ways in which the company can enhance its response strategies.

Consumer protection groups will also benefit from this study. As the market grows, it is important that it is underpinned by confidence on the part of consumers. This study will enable consumer protection groups to understand the mortgage industry and how it works, by outlining the challenges experienced in the industry and how mortgage lenders
respond to those challenges. These groups would be able to consider introducing some mechanisms for ensuring minimum levels of disclosure, complaints handling procedures and adjudication processes.
CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction
This chapter presents theoretical and empirical literature pertinent to the research questions.

2.2 The Theoretical Foundation of the Study
The research was anchored on the Open systems theory, Contingency theory and Resource dependency theory. These theories are discussed below:

2.2.1 The Open Systems Theory
This theory refers simply to the concept that organizations are strongly influenced by their environment (Galbraith & Lawler, 1993). The environment consists of other organizations that exert various forces of an economic, political, or social nature. The environment also provides key resources that sustain the organization and lead to change and survival.

According to Scott (2002), as organizations and communities conduct their business they influence and change their external environments, while at the same time being influenced by external changes in local and global environments. This two-way influential change is known as active adaptive change. Organizations and communities are open systems; changing and influencing each other over time.

People too are open systems. Through their actions they influence and change their external environment, and at the same time are constantly being influenced by changes in the external environment. From an employee’s perspective, the organization itself is their immediate external environment. The prime driver of this change is the increasing rate of
change in people’s values and expectations in the external environment. People are constantly changing their minds about decisions they will make, including what products and services they will buy and how they’ll buy them (Pfeffer & Salancik, 2003). The rate of socio-ecological change is being accelerated by globalisation, deregulation, and technological change. All these factors are combining to produce fierce competition for organizations and communities as well as causing unprecedented turbulence and uncertainty.

2.2.2 The Contingency Theory

The contingency theory is considered a dominant, theoretical, rational, open system model at the structural level of analysis in organization theory (Scott, 1992). The basic assertion of contingency theory is that the environment in which an organization operates determines the best way for it to organize. The position of the organizational theorist is that "the best way to organize depends on the nature of the environment to which the organization relates" (Scott, 1992). Contingency theory has two basic underlying assumptions: First, there is no one best way to organize. Second, any way of organizing is not equally effective (Galbraith, 1973). One of the first contributions of research using a contingency approach was establishing the distinction between 'mechanistic' and 'organic' forms of organization and management (Burns & Stalker, 1961). The mechanistic form was associated with a stable environment and routine technology. The organic form was associated with an unstable or turbulent environment and changing technology. A subsequent study showed that different types of technology or technical systems make different demands on an organization. Environment, technology, age and size emerged as the primary contingency factors.

Researchers often defined additional contingency variables or divided the primary
factors. Mintzberg (1979) identified 11 contingency variables, 4 dealing with the environment, stability, complexity, diversity and hostility. Researchers separated 'Strategic contingency theory' from 'structural contingency theory'. Strategic contingency theorists emphasize the importance of choice and add an intermediate, strategic process. They emphasize the roles of power, politics and individual goals and objectives. Power is both an outcome and determinant providing participants further advantages in the political struggle because of their structural position (Pfeffer & Salancik, 1978). Recent work is addressing multiple contingencies, seeking higher degree of explanation of relationships and attempting integration with other theories (Pennings, 1992). A contingency approach can and has been used to study many areas within organization management, as well as other sciences.

2.2.3 The Resource Dependency Theory

This theory is based upon a set of relationships formed between an organization and its technical environment. These relationships are normally based on the process of exchanging resources. An organization behaves like its environment. In order to understand an organization’s behavior, it is necessary to understand the environment in which the organization is inserted (Pfeffer & Salancik, 1978).

Resource Dependence theories assume that an organization’s behavior is significantly influenced by external pressures. Moreover, an organization is likely to survive to the extent that it can cope with external demands and expectations (Mwankwo & Richardson, 1996). Pfeffer and Salancik (1978) argued that dependence is a measurement of how important resource suppliers are to an organization. This measurement might influence the position of the resource supplier in the organization’s strategic plan. In Pfeffer and
Salancik’s view, any component of the external technical environment should be, to some extent, important for the organization’s survival.

2.3 Environmental Challenges and Strategic Responses

The Kenyan business environment has been undergoing drastic changes, which have affected most industries especially in the last decade. The Government policy on liberalization outlined the reform measures to be undertaken in all sectors of the economy in order to accelerate growth and development. These changes include increased competition, privatization of the public institutions, liberalization of the economy and rapid technological advancement. Organizations have had to adapt their activities and internal configurations to reflect the new external realities. Failure to do this may jeopardize future success of this organization (Aosa, 1996).

Ansoff and Mc Dowell (1990) noted that strategic responses involve change in the organization’s strategic behaviours to assure success in a transforming environment. Pearce and Robinson (2007) defined strategic responses as the set of decisions and actions that result in the formalization and implementation of plans designed to achieve an organization’s objectives. Therefore it is a reaction to what is happening in the economic environment of organizations. Porter (1998), views operational responses as part of a planning process that coordinates operational goals with those of the larger organization. Hence operational issues are mostly concerned with certain broad policies for utilizing the resources of an organization to the best support of its long term competitive strategy.

Porter (1998) observes that for organizations to be able to retain competitive advantage, they need to examine their environment, both internal and external and respond accordingly. Ansoff and McDowell (1990) also point out that the match between its
strategic responsiveness and strategic aggressiveness determines the success of every organization, and how these are matched to the level environmental turbulence. This is because each level of environmental turbulence has different characteristics, requires different strategies and requires different organizational capabilities. Therefore, each level of environmental turbulence requires a matching strategy and the strategy has to be matched by appropriate organizational capability for survival, growth and development. The main role of strategy is to evolve a trajectory or flight path towards the bull’s eye (Mintzberg, 1987). This means that strategy enables organizations to succeed. However, strategy alone is not enough. According to Mintzberg (1987), no shortage of failure can probably be attributed to organizations that got their strategy right while messing up their operations. Execution of strategy is just as important as the creation of it.

2.3.1 Diversification Strategy

Diversification strategy is the process of entering new business markets with new products. This is in response to challenges faced by companies in the form of increased competition and market saturation. Diversification enables a company to give itself a new lifeline, to avoid corporate redundancy. Such efforts may be undertaken either through acquisitions or through extension of the company’s existing capabilities and resources. It seeks to increase profitability through increased sales volumes obtained from new products and new markets. Diversification can occur at the business unit level through expansion into a new segment of an industry, in an industry in which the business is already in, or at the corporate level by entering a promising business outside of the scope of the existing business unit (Ansoff and McDonnell, 1990).

Diversification makes sense when good opportunities can be found outside the present business. Kotler (2000) states that a good opportunity is one in which the industry is
highly attractive and the company has the mix of business strengths to be successful. Three types of diversification are possible. An organization can seek products that have technological and or marketing synergies with existing product lines even though the new products themselves may appeal to a different group of customers. Further the company might search for a new product that could appeal to its current customers even though the new products are technologically correlated to its current product line termed as horizontal diversification. Finally the company might seek new businesses that have no relationships to the company’s current technology, products or markets termed as conglomerate diversification.

2.3.2 Differentiation Strategy

This strategy is one where a company focuses its efforts on providing a unique product or service. Since the product is unique, this strategy provides high customer loyalty. Pearce and Robinson (2007), contend that strategies dependent on differentiation are designed to appeal to customers with a special interest for a particular product attribute. Product differentiation fulfills a customer need and involves tailoring the product or service to the customer and allows organization capture market share. Differentiation aims at developing and marketing of unique products for different customer segments. Using this strategy a company focuses its efforts on providing a unique product or service and due to the uniqueness there is high customer loyalty (Porter, 1980). Differentiation strategy aims to build up competitive advantage by offering unique products characterized by valuable features such as quality, innovation and customer service. Differentiation can be based on the product itself or delivery system. Differentiation can be on the brand, image, technology, features, and customer service and distribution network.
2.3.3 Outsourcing Strategy

This strategy has become a trend in business where companies give up their non-core activities to third party service providers and concentrate on their core business activities (Kerkhoff, 2006). By outsourcing the non-core activities, the company can efficiently channel all its resources towards the production of outputs for which it is in the business. As a result quality production of products/service can leverage its competitive advantage (Kerkhoff, 2006). Instead of spending time managing an activity that is not core to the business, the company hands over to a third party provider to handle it and can be in charge of ensuring efficiency and effectiveness. Outsourcing is the transfer of control of a process or product to an outside supplier. The outside supplier focuses on this specific type of business and has better equipment and technology. Companies outsource parts, components or services that are not one of their critical core processes or parts or differentiating factors (Kerkhoff, 2006).

According to Hook (2004) through outsourcing of non-essential work, the corporation can free valuable resources and focuses on its areas of competitive advantage. To achieve this result the corporation must know its core competence. Outsourcing has fundamentally changed the global business landscape, as competition increases between businesses and budgets wear thin; wise organizations are turning to outsourcing to add value beyond lowering costs. Hook (2004) further argues that organizations outsource due to a number of strategic reasons. The reasons include improving business focus in core activities, gaining access to world class capabilities, accelerating re-engineering benefits, share business risks and redirect resources to more strategic activities.

2.3.4 Innovation Strategy

This is the strategy that taps into the deep insights of an organization human spirit and
knowledge generating a pipeline of ideas that are evaluated, selected and ventured using disciplined tools, methods and processes (Tucker, 2009). Innovation strategy enables organizations to compete favorably in the global market place since it improves business performance of organizations that emphasize it. Ingwe, (2012) sees innovation as the response to environmental turbulence for future opportunities. Research and development departments have the responsibility of generating new ways of doing business through innovations (Ingwe, 2012). He adds that four main factors drive market change and in combination create the need for innovation. These factors are technological advances, changing customer needs, intensified competition and changing business environment. Business environments are changing as markets become more open as the open market economy is embraced by governments. Increased focus on cost cutting through reduction of resources is required for key business processes. Many companies have reengineered their business processes and significant efficiency gains achieved. The shorter product lifecycles and high levels of new product failures have made manufacturing and service companies’ dependent on constant innovation (Ingwe, 2012).

2.3.5 Cost leadership

Cost leadership is a low cost strategy where businesses seek to establish long term competitive advantage by emphasizing and perfecting value chain activities that can be achieved at costs significantly below what competitors are able to match on a sustained basis. This in turn allows the firm to compete primarily by charging a price lower than competitors can match and still stay in business (Pearce and Robinson, 2007). Cost leadership requires aggressive construction of effective and scalable facilities, vigorous pursuit of cost reduction from expenditure, tight cost and overhead control, avoidance of marginal customer accounts and cost minimization in areas like research and development, service sales force and advertising. The low cost position gives the firm a
defense against the rivalry since it could still be able to earn above average returns (Porter, 1980). According to Gachambi (2007), lower costs mean that the firm can still earn returns after competitors have competed their profits away. This strategy guards against substitutes and new entrants due to the favorable position.

2.3.6 Focus Strategy
This is a generic strategy that applies a differentiation strategy approach or a low cost strategy approach or a combination and does so solely in a narrow or focused market niche rather than trying to do so across the broader market. The narrow focus may be geographically defined by product type features, target customer type or some combination of these (Pearce and Robinson, 2007). The business focuses on one or more narrow market segments. The firm gets to know these segments intimately and pursues either cost leadership or differentiation within the target market segments (Kotler, 2007). This strategy provides an opportunity for an enterprise to find and exploit the gap in the market by developing an innovative product that a customer cannot do without. The company has enormous opportunity to develop its own niches and compete against low cost and differentiation enterprises that tend to be larger.

2.3.7 Strategic Alliances
Strategic alliances are applied in response to economic and competition challenges. A strategic alliance is an agreement between two or more parties to pursue a set of agreed upon objectives needed while remaining independent organizations. This form of cooperation lies between mergers and acquisitions and organic growth. These can enable companies to realize many benefits of diversification without having to bear the same level of bureaucratic costs. However, when entering into an alliance, a company does run the risk of giving away key technology to its partner. This risk can be minimized if a
company gets credible commitment from its partner (Hill and Jones, 2001).

2.3.8 Organizational Restructuring

Restructuring is another response to challenges in the environment. Jensen and Meckling (1976), argue that a company is a collection of contractual relationships among various stakeholders, including shareholders, suppliers, employees and customers. Restructuring is the process by which firms change these relationships. What usually drives firms to restructure is some opportunity to increase value or address poor performance. In response to the external environment, companies may opt to restructure in order to address changes in regulatory requirements, and changes in the economic landscape that require companies to seek value from growing market segments.
CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction
The chapter points out the research design, sample design, data collection and data analysis procedures that were used in the study.

3.2 Research Design
The type of research design that was used is case study since it intended to identify response strategies to environmental challenges faced by Housing Finance. Mugenda and Mugenda (2003) define research design as a detailed plan for how the research will be conducted. According to Yin (2003) a case study design should be considered when the focus of the study is to answer “how” and “why” questions, when one cannot manipulate the behaviour of those involved in the study or when the boundaries are not clear between the phenomenon and context.

3.3 Data Collection
Both primary and secondary data sources were used for data collection. The primary data collection method was an Interview Guide, which contained open-ended questions. The interview guide was divided into three sections; A, B and C. Section A addressed the general information about the interviewees and the company, Section B addressed the mortgage industry, while Section C addressed the main issues in order to seek responses to the research question. The researcher also relied on the company’s website, internet, newspapers and other published material as sources of secondary data.

The targeted respondents were the Chief Executive Officer, Finance and Administration Manager, Human Resources Manager, Business Development Manager, Company Secretary, Business Operations Manager and Strategic Projects Manager, Risk
Management Manager, Head of Kenya Building Society, and Head of Housing Finance Foundation. The interview guide was administered through face to face interviews.

3.4 Data Analysis

Mugenda and Mugenda (2003) observe that data analysis is the process of bringing order, structure and meaning to the mass of information collected. Primary data collected through interviews, and the completed interview guides were edited for completeness and consistency. Content analysis was then used to analyze the in-depth qualitative data gathered. Content analysis has been defined as a technique of making inferences by systematically and objectively identifying specific characteristics of messages and using the same to relate to trends.
CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the analysis and findings of the study as set out in the research methodology. The objectives of this study were to find out the challenges facing the mortgage industry in Kenya and to determine the strategic responses adopted by Housing Finance Company of Kenya Limited to such environmental challenges.

4.2 Data on Interviewees

Four out of the targeted 10 senior managers were interviewed. Of the 4, 2 had been in the mortgage industry for more than 5 years, one for 3 years, and 2 for less than one year. Those interviewed were: The Chief Executive Officer, the Business Development Manager, the Risk Management Manager, and the Human Resources Manager.

4.3 Environmental Challenges Facing the Mortgage Industry in Kenya

This section primarily aimed at establishing the various challenges that Housing Finance has encountered in its operations in the mortgage industry in Kenya. This has been viewed at from both internal aspects as well as the external operating challenges. The highlights of the discussion are enumerated herein.

4.3.1. High Mortgage Costs

According to respondents, the mortgage industry faces challenges on the demand for mortgage facilities. While there is absolute growth in demand for housing in Kenya, there is the lack of effective demand. This means that while there is a growing demand for housing, consumers do not have the means to act on the demand as financing is often not available or unaffordable.
Mortgage interest rates in Kenya today are at an average of 14%. This is very prohibitive. The minimum value of a mortgageable property is about Ksh. 4 million, but some flats are now becoming available at about Ksh. 2 million but these are in short supply. The average payment to income ratio is 40% and the average loan maturity is 15 years. Based on this data, a loan of Ksh. 3.2 million would mean 180 monthly installments of Ksh. 42,615. Based on a 40% payment to income, it implies a minimum annual income of Ksh. 1.28 million. This level of income is earned by under 3% of the total population and exclusively in urban areas. Just over 8% of the population in cities would have a sufficient level of income to afford a mortgage loan on the cheapest available property (Walley, 2011).

While many salaried and self employed individuals would like to have a mortgage facility, the closing costs which consist of stamp duty, legal fees, taxes as well as the actual down payment, which amount to as much as 10%, are prohibitive for many potential customers. It is difficult for many individuals to accumulate the sum of cash required for this.

4.3.2 Social Factors

From the respondents, it was clear that there is a lot of fear about mortgages in Kenya and this is partly attributed to history. Kenya in the 90’s went through the political instability of multiparty elections, printing of false money, inflation of 40% and interest rates of over 60%. People lost their homes and businesses collapsed. Many children who are now potential mortgage customers saw the pain their parents went through and they would never want to take out a loan against a house. This is one of the reasons people choose to build incrementally or borrow unsecured loans, borrow from SACCO’s and investment groups, but they will not borrow against their home.
In the rural areas the problem is even bigger, because the land there is family land and in some areas it is not possible to get a title, a mortgage company cannot charge a title. There are also graves on the land, making it impossible to charge such land without causing social unrest.

4.3.3 Cost of Construction

The supply side is about the high cost of the home and the mortgage. Currently, Kenya faces a shortfall of 100,000 homes every year. Only 50,000 new units are built a year, short of the 150,000 required annually. Most of those built for sale target the upper level of the market, meaning the shortfall is much worse for the lower segment of the market.

The cost of construction is very expensive. Kenya is still using bylaws inherited from the United Kingdom who have winters and summers, which requires buildings to have certain expansion sizes. The high cost of inputs facing the housing industry translates into high mortgage costs for buyers. Lack of trunk infrastructure increases costs by up to 12%, further pushing up mortgage costs. This is coupled with the developers need to make profits.

4.3.4 Political Factors

Respondents pointed out that any country that has succeeded in housing has involved the government through government land, subsidies, incentives, infrastructure etc. The mortgage industry players, along with stakeholders in 2007 came up with a new housing bill. The bill was completed in 2007, but it has never gone to parliament due to political issues such as changeover of government, constitution change etc. The bill proposes that the government sets aside 2% of its annual budget into a housing fund and lend it towards
specific levels of the market e.g. lend it towards developers who are doing low cost housing, and also give tax breaks. Developers will always go where there is the highest margin so if they are given tax incentives and holidays they will be willing to go build houses worth Ksh. 1million, which more Kenyans can afford. The 2013/2014 budget allocated about Ksh. 3 billion to the Ministry of Lands, Housing and Urban Development. This amounts to about 0.18% of the total budget, which is very little to solve the housing problem.

4.3.5 Poor Funding of Mortgage Lenders

The unavailability of long term funds and the mismatch between short term deposits and the longer term mortgage loans is a big problem for the industry. Mortgage financing is a capital-intensive venture and mortgage lenders have been relying on short term deposits to fund long term loans, leading to very high interest rates.

4.3.6 Competition in the Industry

Housing Finance is the only mortgage finance company in Kenya and it owns 35% of the mortgage market. KCB, under the S&L company, also owns 35% of the market share. With their combined share of 70% of the market, the two companies are the biggest rivals in the industry. The competition has been quick to duplicate products create by Housing Finance.

4.3.7 High Level of Taxation

Taxation is increasing in the country. Capital gains tax was reintroduced, and the National Construction Authority has come up with a 1% levy on all constructions in the country. KRA is also proposing that deposits paid by customers to a developer to buy a house should be taxed as income even before the house is complete. This means that
prices continue will continue to go up. Respondents felt that housing does not seem the government’s priority and until it is, the housing problem will not be solved.

4.4 Strategic Responses to Environmental Challenges

The researcher sought to find out strategic responses adopted by Housing Finance to environmental challenges facing the industry. The findings indicate that Housing Finance has strategically responded in various ways to the various environmental challenges facing it.

4.4.1 Product Innovation

Product innovation has been key to Housing Finance staying ahead of the competition. With time, its products are replicated by competitors, but its strategy is to keep innovating and stay ahead of the game. The company focuses on creating products that encourage potential customers to save towards home ownership. The First Home Ownership Product (1st Hop) targets people coming into employment for the first time to start a culture of saving. The product entails having a deduction made from the monthly salary to Housing Finance, and this deduction has a tax benefit. It was launched in 2007.

Crossover is another product, and is a high interest earning savings account. Through this account, the company gauges an individual’s ability to save on a monthly basis, so when they are ready to buy a home (crossover), the company can give a discount on interest and a discount on commitment fee because it has gauged the individual’s ability, and also use the savings made for deposit and other closing costs. The history that the company has on the individual makes the verification process easier. The account also has a point system where annually, the account holder receives gifts based on how much they have saved. This account not only helps solve the affordability issue, but also the issue of credit history, which causes mortgage costs to go higher since institutions charge a
premium due to high lending risks of individuals whose histories are not clear. Full operationalization of credit referencing through the CRB is yet to take place to change the situation.

Ezesha is a 105% financing product that also deals with the inability of potential customers to save enough. This product was a first in Kenya, developed when Housing Finance partnered with a South African Firm, Home Loan Guarantors and came up with a scheme where the firm insures the extra amount (above the usual 90%-95%) that Housing Finance lends, and the customer then pays the insurance premium in addition to the mortgage repayment. However, the organization is very clear that this is targeted towards home owners not for investors, and also for the middle income and below. So to qualify for Ezesha, the house has to be valued at Ksh. 10M and below and the buyer must live in it. The goal is to encourage home ownership and the product has been very successful. It initially had a set limit of Ksh. 1B, but Housing Finance is now negotiating for it to be increased. With Komarock phase 5B being launched soon, and houses for up to about Ksh. 9.5M, anyone who is buying to live in it qualifies for Ezesha.

4.4.2 Stakeholder Lobbying
Housing Finance has lobbied the Retirement Benefits Association (RBA) to allow pension holders to use their funds towards obtaining a mortgage facility. The best option negotiated was that individuals can use up to 60% of their pension as security to enable financiers lend more than they would normally lend. For home owners, the company would lend up to 90% or 95% of the value of the house, so owners would still have to pay the 5%, plus legal fees, valuation fees, stamp duty etc. The law was done to enable it lend up to 115% of the value of the house. This means that if the house is valued at Ksh. 5M, the company could then lend up to Ksh. 5.75M. In such a case the Housing Finance
would probably lend about Ksh. 4.5M. The difference of Ksh.1.25M would need a guarantee from the trustees of the pension, such that if anything happened and the company had to reclaim, it would sell the house. If there was any shortfall after sale of the house, only then would it call on the guarantee. However, at the same time, the law on trustees became more onerous. Trustees of pension schemes are personally liable for any issues, meaning they can go to jail. This has caused very few schemes to agree to amend their trust deeds to allow for pension backed mortgages. Housing Finance is therefore looking for alternative options for this facility.

Housing Finance has also been lobbying the government directly and through associations such as Kenya Private Developers Association (KPDA) and Kenya Private Sector Alliance (KEPSA). This has led to developments such as the introduction of the Real Estate Investment Trusts (REITS) legislation, which allows investors to pool funds in a very regulated manner towards real estate projects. Many investors have money but they don't trust Kenyan developers and contractors. With REITS, the CMA has to approve the trustee, the REIT manager, and the whole structure. Investors, especially foreign, will be willing to pump in billions. Interviewees predicted a very big change in the industry, although unfortunately it is most likely to start at the high end. Projects like Two Rivers and Garden City would be likely to be the first beneficiaries.

4.4.3 Organizational Restructuring

Housing Finance, being specifically focussed on housing, and in response to its mission of being the leading integrated solutions enabler for the property industry, has been restructuring its operations along the real estate value chain. This means that it has created companies to focus on specific areas of the value chain, from land acquisition, land development, infrastructure provision, housing and commercial development, all the
way through to selling them, financing the buyers and property management. This has meant creating a holding company or group company, with constituent subsidiary companies that each have their area of focus i.e. banking, property development, property sales, and possibly in future purchase of a construction company or invest in an alternative technology company.

In order to respond to the problem of only very high cost housing being available in the market, in 2012 Housing Finance revived its development arm, Kenya Building Society (KBS). By being in charge of its own developments, the company has been able to sell houses at below market rate to enable more Kenyans own homes. Through KBS, the company is entering into Joint Ventures with landowners, targeting affordable land which is large enough to provide economies of scale and at a cost that would enable houses sell at Ksh. 7million and below. Through it, the company has built and sold out Komarock phase 5A, Precious Gardens in Riruta and Kahawa.

4.4.4 Product Diversification

In a bid to come up with cheaper sources of funding, Housing Finance has diversified its business, and gone into full scale banking by introducing current account, fixed deposit accounts etc. This increases its sources of cheaper funding, the benefits of which are passed on to mortgage customers. However, the benefits will take time to be felt by customers because of the high cost of money in the market. While diversification was necessary, the core business of the organization remains the real estate value chain.

By focusing on the real estate value chain, the company has developed products like asset finance for contractors who need equipment. It has also come up with insurance financing, as every building requires insurance but most developers cannot come up with
the cash upfront, and need insurance premium financing. Housing Finance has therefore come up areas where it can add value to get as much share of wallet from customers as possible.

### 4.4.5 Alternative Funding Sources

Housing Finance in 2010 and 2012 took out corporate bonds, both of which were over subscribed. The corporate bonds help in reducing the asset-liability mismatch i.e. 15 to 20 year loans against 3 to 6 months corporate deposits. They therefore help to mitigate against that risk. However, the challenge is that the rate of return expected in the market has to be competitive, in comparison to the government treasury bills and bonds. For example, in 2010, the government 5 year bond was at about 6.5% so Housing Finance was forced to offer a return of 8.5%. In 2012, it rose to 13%. The problem is that a high return on the bond does not help in bringing down the interest rates or for profit, but it only helps the organization from a funding perspective.

### 4.4.6 Building Innovation

The cost of building houses in Kenya is very high, and part of the cost is the construction materials used in building. Around the world there is a lot of alternative technology which is being used, even by high-end developers. Housing Finance is looking into the possibility of becoming a source of this building technology, and negotiating with foreign investors on ways of partnering on this. It is in the process of setting up factories here in Kenya and build show houses which it will then market by educating the public on the value of using this technology.

### 4.4.7 Housing Finance Foundation
Housing Finance has identified that the building and construction industry is faced by severe skills shortage, with only 25% of workers formally trained. This is despite it being a critical supplier of jobs. As part of its Corporate Social Responsibility, the organization created Housing Finance Foundation, whose goal is to deliver, facilitate and catalyze industry relevant and sustainable practical skills required by the building and construction industry through the creation of an army of 1 million artisans.

4.4.8 Organizational Rebranding

The company rebranded in 2012 from being known as HFCK, which was seen as a poorly performing government type company, to Housing Finance, to reflect a company built on the strength of the old; yet clearly focused on availing new housing opportunities to homeowners, and meeting the growing housing challenges. The company plans, next year as part of its 50th Anniversary celebrations, to rebrand again to make known its new structure and also position itself as more than just a mortgage company and show that it does more, including banking. The company needs to change perceptions in order to enable it grow. This is in response to the very competitive environment and changing customer expectations.

4.4.9 Other Strategies

The respondents indicated that with the changes in structure, and diversification of offering, there has been need to acquire new skills. The organization has brought in individuals with banking experience since it has gone into banking. It has also worked on its IT system with an upgrade that is yet to be launched by the end of 2014. The new system will integrate all its processes, to enable the company become more efficient in processes and in customer service. The company has also engaged in culture change training to inculcate new culture. People have emerged as one of the biggest challenges in
making strategic changes. Resistance to change has been a big factor in executing the various strategies, but has been managed with a mix of motivation, reward and incentive schemes.

4.5 Discussion of Research Findings

Chandler (1962), stated that strategy determines the basic long-term goals of an enterprise, and the adoption of courses of action (strategy as plan of action) and the allocation of resources necessary for carrying out these goals (strategy as resource allocation). The findings show that Housing Finance practices strategic management, and is currently in the middle of its 2012 to 2016 growth strategy, and carries out annual strategic review and planning sessions. This has enabled it to anticipate customer expectations and pioneer new products and innovations in response to the challenging environment it faces.

The findings of this research are in accordance with the open systems theory. The assertion by Scott (2002) that active adaptive change occurs as organizations conduct their business holds. Housing Finance has been greatly influenced by its environment, and has, in turn, influenced the environment around it. Through lobbying, it has changed government policy, and by creating innovative products, has grown the number of people who can own homes through mortgage. Through Joint Ventures and strategic partnerships, it has created new opportunities in the market.

Contingency theorists assert that the environment in which an organization operates determines the best way for it to organize. This theory holds true in the case of Housing Finance. The mortgage industry operates within the wider real estate value chain, and the success of mortgage sales depends on many factors within the value chain. Housing
Finance has engaged in altering its structure in response to its environment, further demonstrating that there is no one best way to organize. Strategic contingency theorists emphasise on the role of power, politics and individual goals and objectives (Pfeffer & Salancik, 1978). In this study, this is demonstrated by the process of culture change, incentive and reward systems put in place to ensure success of the laid out strategies. There was loss of employees who could not cope with the changes taking place.

The findings of this study also support the resource dependence theory. The various resource suppliers in the real estate value chain adopted by Housing Finance play respectively important roles for the organization. By finding ways to work with resource suppliers such as land owners, technology owners, finance suppliers and government the company has been able to leverage on value creation. The various components of the organization’s technical environment play an important role for its survival and Housing Finance has done well in adjusting its strategies to meet expectations.
CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter summarizes and discusses the findings in relation to the statement of the problem and the objectives of the study. It also highlights the limitation of the study and suggestions for further research.

5.2 Summary

The objectives of this study were to determine the environmental challenges facing the mortgage industry in Kenya, and the strategic responses adopted by Housing Finance to such environmental challenges. The study revealed that the mortgage industry in Kenya faces numerous challenges that pose a threat to the profitability of the industry. On its part, Housing Finance has strategically responded to these challenges, and this has enabled it not only survive but grow.

One of the biggest challenges from the environment is the high costs of building and construction in the country, and the high cost of money. These costs cause mortgage costs to go up to a level where they are out of reach for the majority of Kenyans. Housing Finance has responded to the cost challenge by issuing corporate bonds to provide it with more funds to lend out, at a relatively cheaper rate. This has helped in bridging the asset-liability mismatch. It is also researching into alternative building technology, which will bring down building costs and hence mortgage costs. It has plans to possibly purchase a firm that offers this technology. The company has also partnered with other parties such as landowners to put up largescale projects which reap economies of scale, with a view to selling houses as lower costs. It has been successful, and continues to apply this strategy.
Political factors are another big environmental challenge. Housing Finance has been at the forefront of lobbying for matters to do with housing in the country, and pushing for more government attention to the industry. The result of this has been the creation of pension backed mortgages, which allow pension holders to use up to 60% of their pension as security to receive a higher mortgage loan amount. The introduction of REITS is also a big step forward for the industry and will see more investment in the industry, which should eventually reach the lower income segments of the population.

Economic factors also pose major challenges to the industry. The rising inflation level means that individuals have less to spend. The high level of taxation is also a big impediment to the growth of the industry. With new taxes being levied such as the 1% levy on all constructions, capital gains tax among others, the industry’s challenges are not waning. Housing Finance has responded to economic factors by finding ways to enable the customer to save and offering a higher percentage on loans. It has done so through product development, developing products such as 105% financing through Ezesha, offering young people the chance to save for mortgage tax free through 1st Hop, and a high interest earning savings account through Crossover. The company has also diversified its offering into full scale banking to allow for new cheaper sources of funding that will eventually trickle down to customers.

Competition also emerged as a major challenge. Housing Finance has responded to this challenge by restructuring. By focusing on the entire real estate value chain, Housing Finance is expressing its focus on its core business, and extending itself out of competitors reach, all of who are focussed on the banking industry. This means that it is able to create new avenues to engage in business with developers, land owners, contractors and other potential customers. It has also been a market leader in creating new
products, which are quickly replicated by competitors. The company has also rebranded to Housing Finance, to signal its new commitment to enabling more Kenyans own homes. It is soon to rebrand again, to reflect its new structure and offering.

5.3 Conclusion

From the study’s findings, the researcher concludes that the mortgage industry in Kenya faces many environmental challenges, arising from PESTEL factors. These factors pose a challenge to the survival and growth of companies in the industry. It was established that the key environmental challenge facing the mortgage industry in Kenya is high mortgage costs arising from high cost of money, expensive building and construction methods and materials, high cost of land and taxation. Generally there is a lack of focus by the government on the housing sector. The researcher further concludes that Housing Finance has responded strategically to the environmental challenges it faces. It has done so through product innovation, diversification, restructuring, lobbying the government, and seeking joint ventures and partnerships and competitively hiring the right talent. Strategic planning is at the core of the organization’s activities, and this has provided it with a long term view of the industry and the business.

The researcher further concludes that Housing Finance’s strategy of focusing on the real estate value chain is a strategy that may work for them or eventually become a problem. The company has focussed on creating value along the real estate value chain. While this strategy enables it mitigate many of the risks from the environment, the company may face value erosion by certain aspects of the value chain that have low margins. Trying to do everything along the value chain has the potential to be detrimental to the business in terms of provision of expertise and competitiveness, as it is difficult to be good at everything. As it considers the way forward, the company should think about outsourcing
needs such as construction and technology rather than creating its own capabilities. Creating more strategic alliances and joint ventures on projects will allow the company to focus on its expertise and build capacity for better competitiveness.

5.3 Implications of the Study

This study will be useful to policy makers, government and regulators in outlining the challenges that the mortgage industry in Kenya is facing. From the study, it is clear that government policy is a big challenge in the industry, and it will influence policy makers to address the issues outlined in the study.

The research will also be of value to the staff at Housing Finance, in enabling an understanding of the reasons behind decisions that are made i.e. that the organization has to keep evolving in response to the environment. This will allow for better acceptance, and even prediction or suggestions of changes that should happen to enable the organization to overcome environmental challenges.

5.4 Limitations of the Study

Time was a limiting factor. The researcher is in full time employment and therefore did not have adequate time especially in the collection of data. Limited resources on the part of the researcher were another limitation. The research lacked adequate funding for conducting the research. The respondents were also quite guarded in their responses, due to suspicion that such study could expose their competitive advantage to their competitors.
5.5 Suggestions for Further Research

The study focussed on the environmental challenges facing the mortgage industry in Kenya, and how Housing Finance has responded to these challenges. However, the mortgage industry is one aspect of the larger housing sector in Kenya. Issues concerned with the housing sector directly affect the mortgage industry. It would therefore be of value to study the larger housing sector as a whole, to establish the environmental challenges facing the sector and possible solutions to such challenges.

The study further recommends research on successful mortgage industry in a country that is within Kenya’s development range. This would be useful in order to provide a view on some of the challenges that are faced, and the strategic responses that were employed in those countries, and that may be employed in Kenya to grow the industry further.
REFERENCES


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APPENDICES

APPENDIX 1: INTERVIEW GUIDE

This Interview Guide seeks to identify the various Mortgage Industry challenges that have affected Housing Finance Company of Kenya Limited and the kind of strategic responses the company has adopted in order to survive in the Mortgage Industry in Kenya.

SECTION A: GENERAL INFORMATION

1. Respondent’s Job Title in the Company______________________________
2. Respondent’s Department/Section______________________________
3. Respondent’s duration of service in the Company______________________________

SECTION B: MORTGAGE INDUSTRY

Which challenges have you observed in each of the following environmental factors that affect the company? Please explain

a. Regualtory Factors
b. Competition in the industry
c. Rise in inflation
d. Changing customer expectations
e. Employee expectations
f. Technological changes
g. Political factors
h. Social factors
i. Economic factors
j. Other industry environment factors

SECTION C: STRATEGIC RESPONSES

1. What do you think have been the implications of the challenges for each of the environmental factors in (Section B) above?

2. For each of the challenges mentioned in (Section B) above, how has your company strategically responded to them?

3. Has your company developed any internal capability to effectively and successfully execute the strategic responses explained in (Section B) above?

4. Overall do you think the company has competitively positioned itself favourably to environmental challenges? Please explain how?

5. How have the strategic responses adopted by Housing Finance Company of Kenya Limited influenced achieving profits, increased sales and large clientele base compared to its competitors?

6. Have there been any challenges in implementation of the above mentioned strategic responses by the bank? If yes, what are these challenges and how what are organization’s strategic responses?
APPENDIX 2: LETTER OF INTRODUCTION

UNIVERSITY OF NAIROBI
SCHOOL OF BUSINESS
MBA PROGRAMME

DATE: 10 SEP 2014

TO WHOM IT MAY CONCERN

The bearer of this letter, ESTHER NYAMBURA, with Registration No. P61-60226/2013, is a bona fide continuing student in the Master of Business Administration (MBA) degree program in this University. He/she is required to submit as part of his/her coursework assessment a research project report on a management problem. We would like the students to do their projects on real problems affecting firms in Kenya. We would, therefore, appreciate your assistance to enable him/her collect data in your organization. The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

PATRICK NYABUTO
MBA ADMINISTRATOR
SCHOOL OF BUSINESS