ACHIEVING COMPETITIVE ADVANTAGE THROUGH OUTSOURCING AT NATIONAL BANK OF KENYA LIMITED

BY:

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DECLARATION

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

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This research project has been submitted for examinations with my approval as the university supervisor.

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DEDICATION

To my loving husband Robert Kabiru Nderitu, whose wisdom and counsel has been the cornerstone in my quest for academic excellence.

To my parents Mr. & Mrs. Dominic Mutua, for always believing in me. Thank you for all the support provided.

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ABSTRACT

Outsourcing is growing at a rapid rate throughout the world because organizations view it as a way to achieve strategic goals, improve customer satisfaction and provide other efficiency and effectiveness improvements. Outsourcing assists management focus all their intellectual resources, expertise and time on the distinctive competencies that give the firm an edge in the market. Focusing on the core activities ensures collective learning especially on how to co-ordinate diverse production skills and integrates multiple streams of technologies. The purpose of the study was to determine the role of outsourcing services as a source of competitive advantage at the National Bank of Kenya. The study adopted a case study research design in which an interview guide was used to collect data and content analysis was used in analyzing the data. The result findings show that as a result of outsourcing, the bank has gained some level of competitiveness and also a competitive advantage over other players in the banking industry. The bank has gained good competitiveness such that it currently collects around 45% of all KRA remittances and with the high level of collection, it has been able to receive proportionately high commissions from the transactions. The bank has however faced a number of challenges in the course of servicing the outsourced services. These challenges include the small number of transaction that a client might request which will be uneconomical to the bank since for the cost of processing to be covered, there should be a minimum number of outsourced transactions that a client should offer. The study recommended further research to be carried out on other banks in Kenya and/or East Africa.

CHAPTER ONE: INTRODUCTION

1.1 Background of the study

Strategic outsourcing is the process of engaging the services of a provider to manage essential tasks that would otherwise be managed by in-house personnel. It is a strategy that concentrates an organization's resources on its core competencies allowing the organization to achieve a definable preeminence and provide a unique value for customers (Behara, Gundersen, and Capozzoli, 1995). This is often done to allow a business to arrange the use of its assets to best advantage, and allow the company to move closer to the achievement of its goals. The strategic goals of outsourcing are improved efficiencies, lower costs, improved flexibility, higher quality, and a greater ability to achieve a competitive advantage (Momme, 2002).

The ultimate strategic goal is to develop core competencies that develop into barriers of entry that make it difficult for competition to copy. By focusing on core competencies, and utilizing qualified vendors to provide process that are not one of the organization's core competencies, the organization's risks can be shared with its suppliers, and minimized. Core competencies are also the innovative combinations of knowledge, special skills, proprietary technologies, information, and unique operating methods that provide the product or the service that the customer value and want to buy (Greaver, 1999).

Outsourcing goes beyond the mere common purchasing and consulting contracts because not only are the activities transferred, but also resources that make the activities, occur. The resources include people, facilities, equipment, technology, and other assets. An entire function may be outsourced or some elements of an activity may be outsourced, with the rest of the activities being kept in-house (Jacobs, 2009).

Identifying a function as a potential outsourcing target, and then breaking that function into its components, allows decision makers to determine which activities are strategic or critical and should remain in-house and which can be outsourced. Reasons why companies decide to outsource vary greatly. Outsourcing may be used to gain competitive advantage and has been adopted widely. Companies are increasingly seeking outside firms to perform activities previously conducted in-house in order to achieve time, progress and cost advantage. The act of outsourcing makes sense for firms that lack the necessary economies of scale, skills or technology to perform certain functions quickly and efficiently (Jacobs, 2009). Though outsourcing has been reported as a success story, the way in which it has been implemented seems to be of key importance. Banks are focusing on outsourcing as a management strategy to delegate major non-core functions to specialized service providers. Outsourcing represents a significant shift in the way organizations manage and delegate their business support activities (Lutta, 2003).

1.1.1 Competitive Advantage

A competitive advantage is an advantage gained over competitors by offering customers greater value, either through lower prices or by providing additional benefits and service that justify similar or possibly higher prices. Competitive advantage is what enables a business organization to thrive. It is the objective of strategy. It is the combination of elements in the business model which enables a business to better satisfy the needs in its environment, earning economic rents in the process (Porter, 1980).

A firm has a competitive advantage when it is implementing value creating strategy not simultaneously being implemented by any current or potential competitors. A firm has a sustained advantage when competitors are unable to duplicate the benefits of this strategy. A firm enjoying a sustained competitive advantage may experience these major shifts in the structure of competition, and may see its competitive advantages nullified by such changes. However, a sustained competitive advantage is not nullified through competing firms duplicating the benefits of that competitive advantage (Barney, 1991).

1.1.2 Concept of outsourcing

The concept of outsourcing came from the American terminology "outside resourcing", meaning to get resources from the outside. The term was later used in the economic terminology to indicate the use of external sources to develop the business, which typically were using their internal resources. Outsourcing became common once vertical and conglomerate mergers started replacing the more traditional horizontal mergers. The reason cited was that of core competence wherein the 'acquirer' continued to focus on its main operations and outsourced certain activities. The purpose of outsourcing was to maintain the acquirer's competitive advantage (Quelin and Duhamel, 2003).

Porter's Five Forces were the guiding principles behind this strategic decision. The reasoning was that a firm should not abandon its competitive strategy. By focusing on its strategy, the company could maintain its competitive advantage (Porter, 1980).

Porter (1980) introduced five force analyses and linked it to generic strategies. In five forces analysis, he identified the forces that shape a firm's strategic environment; threat of new entrants, bargaining power of buyers, bargaining power of suppliers, threat of substitute products or services and rivalry among existing competitors. He observed that a firm can use these forces to obtain a sustainable competitive advantage in broad (industry wide) or narrow (market segment) scope either by gaining cost advantage or differentiation (product uniqueness) strength. Porter, further, noted that three generic strategies namely: cost leadership, differentiation, and focus result when applying the two strengths at the business unit level (Porter, 1980).

Outsourcing, once used mainly for downsizing and cost reduction at major corporations, should be used as a strategic tool to deliver a forceful impact on corporate growth and financial stability. By outsourcing non-essential work, the corporation can free valuable resources and focus on its areas of competitive advantage. To achieve that result, the corporation must know its core competencies, the type of work within the organization, and manage the outsourcing process. The unit of competitive advantage work is work that should be retained within total corporate control and often described as "in-house" work. This is associated with the defined areas of core competency (Hook, 1998).

Banks all over the world are experiencing stiff competition from their competitors. To gain a competitive edge, they need to be flexible and innovative in their modes of operations. Lyson and Farrington (2006) perceive competitive advantage as a special edge that enables an organization to deal with market dynamics and environmental forces better than its competitors do. Intense competition and market saturation are forcing Kenyan banks to access new revenue streams. They are expanding their array of products through services and increasing focus on customer loyalty programs.

1.1.3 Kenyan Banking Industry

The Banking industry in Kenya is governed by the Companies Act, the Banking Act, the Central Bank of Kenya Act and the various prudential guidelines issued by the Central Bank of Kenya (CBK). The banking sector was liberalized in 1995 and exchange controls lifted. The CBK, which falls under the Minister for Finance docket, is responsible for formulating and implementing monetary policy and fostering the liquidity, solvency and proper functioning of the financial system. There are forty four banking and non bank institutions, fifteen micro finance institutions and one hundred and nine foreign exchange bureaus. The banks have come together under the Kenya Bankers Association (KBA), which serves as a lobby for the banking sector's interest. Over the last few years, the Banking sector in Kenya has continued to grow in assets, deposits, profitability and products offering. The banks have realized tremendous growth in the last five years and have expanded to the East African region. The banking industry in Kenya has also involved itself in automation, moving from the traditional banking to better meet the growing complex needs of their customer and globalization challenges (www.pwc.com).

There has been increased competition from local banks as well as international banks, some of which are new players in the country. This has served the Kenyan economy well as the customers and shareholders are the ones who have benefited the most.

1.1.4 National Bank of Kenya

National Bank of Kenya (NBK) is a commercial bank in Kenya and a large financial service provider serving individuals, small to medium companies, businesses (SMEs) and large corporations. The bank was established in 1968 as a 100% government-owned financial institution. In 1994, the Kenyan Government reduced its shareholding to 68% by selling 32% shareholding to the public. The government further divested from NBK over the years, until its present shareholding of 22.5%, as of October 2010. NBK operates one subsidiary Company, NatBank Trustee and Investment Services Limited incorporated in Kenya on 21st July 1995 with a Share Capital of Ksh.10 Million (www.nationalbank.co.ke).

NBK provides banking, financial, and related services to the retail and corporate business segments in Kenya. Its deposit and other accounts include current, national saver, student, Pinnacle, Vision, foreign currency, Taifa, Al-mumin, wages, Uchuuzi SME transactional current, and Super Chama accounts, as well as call deposits and fixed deposits. The company's lending products portfolio comprises loans, overdrafts, personal loans to salaried customers, asset finance, mortgages, NBK study loans, and salary advances. It operates 41 outlets. The company is headquartered in Nairobi, Kenya.

Several organizations and institutions have outsourced the services of NBK, to make it easier for their customers to be served efficiently. These organizations include Kenya Revenue Authority (KRA), Kenya Airways, NHIF, Kenya Power, and institutions like Kenyatta University, KASNEB, and a variety of secondary schools across the country.

1.2 Research Problem

Today organizations in all spheres compete to deliver value. Value is the ability to meet or exceed the needs of customers, and do so efficiently. Competitive advantage is critical for an organization's success. Strategies that are commonly used for competitive advantage are differentiation, cost leadership, innovation, diversification, outsourcing, growth and alliances. Competitive strategy refers to how a company competes in a particular business. It is concerned with how a company can gain a competitive advantage through a distinctive way of competing.

Kenya's banking sector is a cut-throat business arena with forty four players including multinationals all competing in the same market. The banking industry in Kenya has revolutionized over the last few years, and traditional banking has moved to better meet the growing complex needs of their customers because of stiff competition. NBK being one of the players in the market is utilizing various competitive strategies to have an edge over its competitors as well as to sustain profits.

Previous studies on outsourcing focus mostly on outsourcing human resource and information technology so as to free up organizations to focus on their core competencies. Serem (2005), states that outsourcing as a practice is adopted for different reasons, the most outstanding being the organization's deliberate effort to focus on core business. Wandabwa (2006) affirms that outsourcing is widely used in the banking sector and managing outsourced business processes is the key to providing competitive services so as to shift focus on core activities. A study by PriceWaterhouseCoopers (1999), established that outsourcing has moved markedly from attending a single function more efficiently, to reconfiguring a whole process in order to attain greater shareholder value across the enterprise. In effect emphasis is shifting from outsourcing parts, facilities and components towards outsourcing the intellectual based systems. Though studies have been done at NBK on competitive strategies, they have not focused on strategic outsourcing as a tool for competitive advantage. How is National Bank of Kenya Limited utilizing outsourcing in achieving competitive advantage?

1.3 Research Objectives

This study had two objectives. These were:

i. To establish how NBK is utilizing outsourcing in achieving competitive advantage,

ii. To determine the challenges influencing NBK to develop outsourcing as a competitive advantage.

1.4 Value of the study

This study may benefit all organizations and corporations that will aspire to outsource in order to achieve competitive advantage. These organizations will be challenged to evaluate what they do best internally and/ or externally, and how to weave the two together in a way that maximizes value for them.

The findings will have important practical implications to NBK top managers and others responsible for the development, implementation, or execution of strategies in the organization. It will help management know if the strategy is viable in competing

in the banking industry. This project paper should help in evaluating if the reasons to outsource are favorable, and if the strategy is suitable for the organization.

It will also be of importance to future researchers and academicians who would wish to conduct further research on the trend. There have been a variety of researches done on strategic outsourcing. The research is not exhaustive as strategic outsourcing is dynamic.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter highlights the major issues relating to the influence of outsourcing as a source of competitive advantage, outsourcing strategy and the role of outsourcing strategy as a source of competitive advantage.

2.2 Competitive Advantage

When a firm sustains profits that exceed the average for its industry, the firm is said to possess a competitive advantage over its rivals. The goal of such a business strategy is to achieve a sustainable competitive advantage. A competitive advantage exists when the firm is able to deliver the same benefits as competitors but at a lower cost, or deliver benefits that exceed those of competing products. Thus, a competitive advantage enables the firm to create superior value for its customers and superior profits for itself (Barney, 1991).

According to the resource-based view, in order to develop a competitive advantage the firm must have resources and capabilities that are superior to those of its competitors. Without this superiority, the competitors simply could replicate what the firm was doing and any advantage quickly would disappear (Grant, 1991). The firm's resources and capabilities together form its distinctive competencies. These competencies enable innovation, efficiency, quality, and customer responsiveness, all of which can be leveraged to create a cost advantage or a differentiation advantage. Cost and differentiation advantages are known as positional advantages since they describe the firm's position in the industry as a leader in either cost or differentiation (Porter, 1980).

A resource-based view emphasizes that a firm utilizes its resources and capabilities to create a competitive advantage that ultimately results in superior value creation.

Achieving a competitive advantage allows the firm to earn economic rents or above average returns. In turn, this focuses attention on how firms achieve and sustain advantages (Fahy and Smithee, 1999). According to Fahy and Smithee (1999), the resource based view (RBV) contends that the answer to this question lies in the possession of certain key resources, that is, resources that have characteristics such as value, barriers to duplication and appropriability. A sustainable competitive advantage can be obtained if the firm effectively deploys these resources in its product markets. Therefore, the RBV emphasises strategic choice, charging the firm's management with the important tasks of identifying, developing and deploying key resources to maximise returns (Fahy and Smithee, 1999).

Generally, the process of strategic management involves the thorough analysis of the organisation's external environment and its internal capabilities, which requires the careful identification and management of it's competencies to support the selected strategies. Kenyan Banks are using the following strategies to respond to competition in the banking industry: product offering diversification, branch and regional expansion, relationship marketing, financing, customer-care, innovation, and information technology strategies. NBK has also been using the above strategies and strategic outsourcing is an additional strategy to counter competition (Momanyi, 2010).

2.3 Outsourcing Strategy

The decision to outsource is a major strategic one for most companies, since it involves weighing the potential cost savings against the consequences of a loss in control over the product or service. According to Quinn and Hilmer (1994), a major strategic concept in outsourcing decisions is core competence. There are three basic tests that can be employed to identify the core competences of an organization. First a core competence should provide potential access to a wide variety of markets. A core competence should also make a significant contribution to the perceived benefits as experienced by the customer of the product. Finally, a core competence should be difficult to imitate by competitors.

For the meaningful analysis of outsourcing various theoretical insights are helpful. Transaction Cost Theory (TCT) originates from economic perspective and Resource Based View (RBV) is heavily applied in strategic management. Transaction costs are often disregarded because of the difficulty in quantifying the costs. Firms need to consider both the production and transaction costs in relation to outsourcing (Lacity and Willcocks, 1994). Other unexpected hidden costs are related to activities such as contractual amendment, unexpected transition and management, lock-in and disputes and litigations (Bahli and Rivard, 2003). In addition to the production costs, firms pay close attention to the potential increase in all other transaction-related.

Resource-Based View argues that a firm has the ability to achieve and sustain competitive advantage if it posses resources that are valuable, rare, imperfectly imitable and non substitutable (Barney, 1991). Not all resources are strategically relevant within an organization. The goal of an organization is to ensure it has access to and control of valuable resources by developing and securing all the relevant resources either internally or externally (Das and Teng, 2000). If a firm possesses critical resources that have strategic value, it is better to retain the activity in-house. On the contrary, if the strategic value of target activities is low and no internal resources are available to perform such activities, it is beneficial for the company to outsource them (Roy and Aubert, 2001). For the sustainable competitive advantages, firms are forced to rely on a multitude of outside suppliers for parts, software, knowhow and sales and in doing so gain access to valuable resources and external capabilities.

2.4 Gaining Competitive Advantage through outsourcing

An outsourcing strategy creates a competitive advantage if three criteria are met. First, if implemented it must become a major or significant strength or capability of the organization. Second, it must be unique and proprietary to the organization.

Third, the advantage provided by the outsourcing must be sustainable for at least three years. A competitive advantage means an organization does something important much better than its competitors (Porter, 1980).

A common approach used to identify opportunities to change the structure and profitability of an industry is to examine five competitive forces. Michael Porter argued that the power of buyers, the power of suppliers, the threat of new entrants, the threat of substitute products, and the rivalry among existing competitors determines the profitability of an industry. How a company uses strategic outsourcing can affect each of the five competitive forces and can create the need and opportunity for change (Porter, 1985).

For example, outsourcing has altered the bargaining relationships between companies and their suppliers, channels, and buyers. Outsourcing can reduce the power of buyers and suppliers. It can erect new barriers that reduce the threat of entrants. Outsourcing can help differentiate products and services and reduce the threat from substitutes. Also, it can help managers reduce the cost of rivalry actions and in some cases reduce the need for competitive actions and reactions. Some firms have no competitive advantage. Firms can achieve a competitive advantage by making strategic changes and can lose a competitive advantage when competitors make strategic changes.

2.5 History of outsourcing

The idea of outsourcing is not new. It has been utilized traditionally, but on menial chores. Now it is currently a very popular strategy, commonly used by many companies. The history of outsourcing may have started out with very sordid stories based on world history. The story line has changed and outsourcing will continue to grow through time.

In the mid 1800's at the start of the Industrial Revolution, financiers and capitalists who needed to put up their factories needed engineers and machinists. During this period of world history, large scale outsourcing activity was conducted by colonizers. Food production, resource extraction and human labor were outsourced from other countries that became colonies of powerful countries (Presnell, 2006).

Since the Industrial Revolution, companies have grappled with how they can exploit their competitive advantage to increase their markets and their profits. The model for most of the 20th century was a large integrated company that can own, manage, and directly control its assets. In the 1950s and 1960s, the rallying cry was a diversification to broaden corporate bases and take advantage of economies of scale. By diversifying, companies expected to protect profits, even though expansion required multiple layers of management (Vining and Globerman's, 1999).

Outsourcing was not formally identified as a business strategy until 1989 (Mullin, 1996). However, most organizations were not totally self-sufficient; they outsourced those functions for which they had no competency internally. Publishers, for example, have often purchased composition, printing, and fulfillment services. The use of external suppliers for these essential but ancillary services might be termed as the baseline stage in the evolution of outsourcing.

Outsourcing support services is the next stage. In the 1990s, as organizations began to focus more on cost-saving measures, they started to outsource those functions necessary to run a company but not related specifically to the core business. Managers contracted with emerging service companies to deliver accounting, human resources, data processing, internal mail distribution, security, plant maintenance, and the like as a matter of good housekeeping. Outsourcing components to affect cost savings in key functions is yet another stage as managers seek to improve their finances (Handfield, 2006).

The current stage in the evolution of outsourcing is the development of strategic partnerships. Until recently it had been axiomatic that no organization would outsource core competencies, those functions that give the company a strategic advantage or make it unique. Often a core competency is also defined as any function that gets close to customers. In the 1990s, outsourcing some core functions was a good strategy. For example, some organizations outsourced customer service, precisely because it was so important.

Eastman Kodak's decision to outsource the information technology systems that undergird its business was considered revolutionary in 1989, but it was actually the result of rethinking what their business was about. They were quickly followed by dozens of major corporations whose managers had determined it was not necessary to own the technology to get access to information they needed. The focus today is less on ownership and more on developing strategic partnerships to bring about enhanced results. Consequently, organizations are likely to select outsourcing more on the basis of who can deliver more effective results for a specific function than on whether the function is core or commodity.

2.6 Outsourcing Benefits and Risks

Increasingly, with rapid wealth growth of emerging global economies, the basis of competitive advantage is changing from internal capacities to network capabilities (McEvily and Marcus, 2005). In this highly competitive global environment, outsourcing is more than a tool for functional value extension but strategic priority practice. Outsourcing may reduce operation costs and free up asset (Harland and Knight 2005). In the early 1980s, companies started outsourcing non-core activities to suppliers for the purpose of securing specialized expertise and lower costs. Firms have moved their internal manufacturing and operations to lower cost countries to seek competitive advantage.

Outsourcing benefits include lower cost, more investment on core competencies, flexibility, reduction assets and complementary capabilities. While outsourcing is associated with various benefits, it can also be a serious risk factor (Bahli and Rivard, 2003). Examples of outsourcing risks are interface within activities, loss of competitive base, opportunistic behavior, rising transaction and coordination costs, limited learning and innovation and higher procurement costs in relation to the fluctuating currency exchange rates. If firms only focus on achieving short-term benefits of outsourcing without considering these risk factors, they may fail to access original goals of outsourcing. Firms need to carefully consider balancing the benefits and risks to maximize the outsourcing effects on their long-term competitive advantages (Rothaermel and Hitt, 2006). In this sense, firm's approach to outsourcing is becoming increasingly strategic.

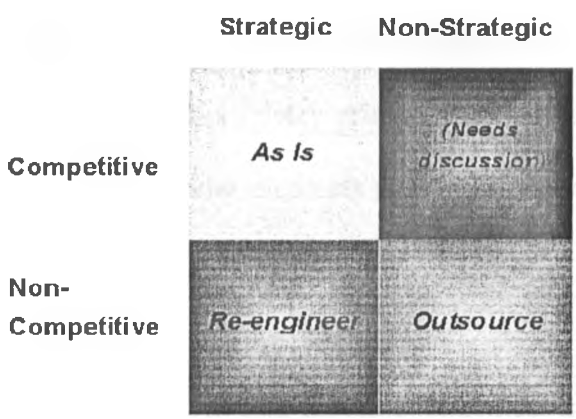
2.7 Evaluation of activities to outsource

Many organizations continue to make outsourcing decisions on a piecemeal basis and fail to develop outsourcing strategies for their processes that allow them to compete in the global economy (Gottfredson, 2005). In many cases, the choice of which parts of the business to outsource is based on ascertaining what will save most on overhead costs, rather than how the decision impacts upon the long-term capabilities of the organization. In some instances, organizations are outsourcing processes that are critical to competitive advantage and over time are relinquishing important knowledge sets and capabilities.

Conventional wisdom regarding the outsourcing decision states that you should outsource your non-core business activities. The difficulty with this approach, however, is that it provides no guidance for deciding which activities are non-core. Ultimately, in many organizations adopting this approach, the discussion about what is "core" and what is "non-core" ends up being highly subjective, and in the end, one person's opinion ends up prevailing over another's.

A better approach, and the one that Price Waterhouse Coopers typically adopts in advising clients about the outsourcing decision is to look at the decision in terms of a two-by-two matrix, as shown below.

Figure 1, Price Waterhouse Coopers two-by-two matrix



Source: Sandy Dunn, *Maintenance Outsourcing – Critical Issues*

(Pricewaterhouse Coopers, 2000)

In this diagram, PWC considers the outsourcing decision along two dimensions. The first, Strategic/ Non-Strategic, considers how important the activity proposed for outsourcing is to the organization in achieving long term strategic competitive advantage in its chosen marketplace. In terms of maintenance, this will clearly vary from organization to organization, depending on the industry that it competes in, and its chosen strategy for competing in that industry.

For example, for a contract mining organization, where competitive advantage in the industry is largely driven by being the lowest cost producer, maintenance clearly is of strategic competitive importance to the firm. Outsourcing maintenance in this environment would, in effect, be handing over control of this potential source of competitive advantage to an external party. On the other hand, maintenance to a hospital may be of less strategic importance, and therefore could, potentially be a candidate for outsourcing (Price Waterhouse Coopers, 1999).

The second dimension, competitive/ non-competitive, relates to how competitively the function being considered for outsourcing is currently being performed compared to the external competitive marketplace. This relates primarily to the cost of the service, but could also be extended to include service elements such as response time.

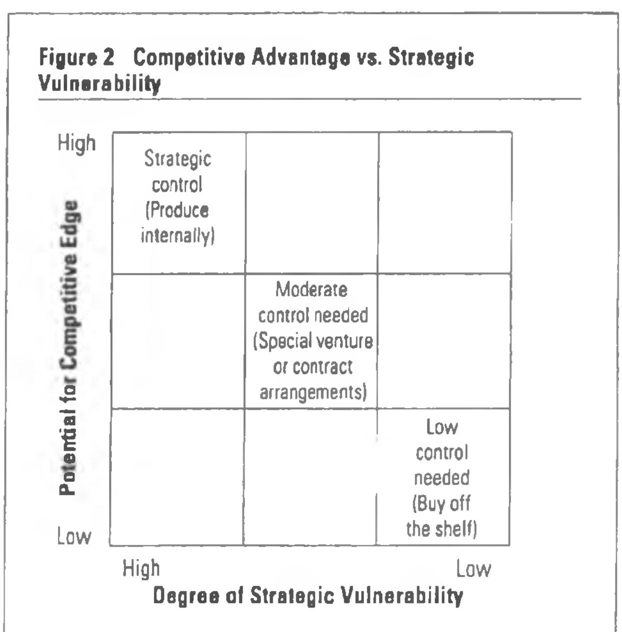
Putting the two elements together gives four possible outcomes; those functions that are of strategic importance to the firm, and which are currently being performed competitively require no further action, the status quo should be retained. Those functions that are of strategic importance to the firm, but which are not currently being performed competitively with the external marketplace should not (in the long run) be outsourced. Instead, a better long-term option is to re-engineer them to ensure that they are performed at a competitive cost. It is possible that, as an interim measure to speed the transition process, a tactical decision is made to outsource the function in the short term, but as stated previously, in the long term the function, as a source of potential competitive advantage, should be retained in-house (Price Waterhouse Coopers, 1999).

Those functions that are not of strategic importance to the firm, and which are not currently being performed competitively with the external marketplace should be outsourced. There is little value in investing in improving this function.

The final combination, those functions that are not of strategic importance to the firm, but which are being performed competitively with the external marketplace is more interesting. In view of the risks associated with the decision to outsource, managers must be cautious when deciding to outsource (Price Waterhouse Coopers, 1999).

Quinn and Hilmer (1994) developed two dimensions for classifying the many different activities that a firm deals with, namely the potential for competitive edge and the degree of strategic vulnerability.

Figure 2, Strategic sourcing, competitive advantage versus vulnerability



Source: Quinn, J. B. and Hilmer, F. (1994). Strategic Outsourcing. *Sloan Management Review,* summer, 43-55.

Quinn & Hilmer (1994) talk about activities in general without making an explicit difference between parts and intangibles. The model suggests that activities with a high potential for competitive edge and a high degree of strategic vulnerability should be realized in house. Moderate strategic vulnerability and moderate potential for competitive edge represent activities that call for a range of relationships like short-term contracts, call options, long term contracts, retainer, joint development, partial ownership or full ownership in relation to the suppliers. Activities with low vulnerability and low potential for competitive edge call for arm's-length relationships with the suppliers. A careful analysis of the model reveals that it considers only three possibilities out of a total of nine.

2.8 Current Trends in Outsourcing

Financial firms have entered into outsourcing arrangements for many years, albeit not to the extent seen in the recent past. For example, in the securities industry, since the 1970s, firms have outsourced quasi-clerical activity, such as the printing and storage of records. This was undertaken because of the comparative cost savings.

As technology has evolved, outsourcing of information services has become more common. In the 1980s and 1990s, such deals tended to be large scale and often involved the outsourcing of whole IT divisions primarily based on cost and the importance of remaining up to date with rapidly evolving technology (Behara, Gundersen, and Capozzoli, 1995).

Subsequently we have seen a growth of outsourcing in more strategic areas such as human resources and some have observed the trend of "business processing outsourcing," (BPO) i.e., end-to-end outsourcing of a business line or process in its entirety. BPOs also mean that the relationship between the outsourcer and the third party changes somewhat as the latter becomes more of a strategic partner than a traditional supplier.

Another major trend in outsourcing that appears to have gained momentum is off-shoring which means effectively outsourcing activities beyond national borders. Many conglomerates are trying to create global efficiencies by basing transaction processing and call centers offshore. Arrangements are sometimes entered into with unrelated parties, while in other cases the outsourcing firm establishes its own off-shore base to provide services (Kavanagh, 1997).

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the methodology that was used to carry out the research. It details the research design, data collection methods, and data analysis methods.

3.2 Research Design

According to Hartley (2004), research design is the argument for the logical steps taken to link the research question(s) and issues to data collection, data analysis and data interpretation in a coherent way.

The research was conducted through a case study. Yin (1984) defines a case study research method as an empirical inquiry that investigates a contemporary phenomenon within its real-life context; when the boundaries between phenomenon and context are not clearly evident; and in which multiple sources of evidence are used. The study sought to establish how National Bank of Kenya Limited has achieved competitiveness through outsourcing.

3.3 Data Collection

Primary and secondary data collection method was used in this study. Primary data was collected using an interview guide, in particular the semi-structured type. Secondary data was also collected from NBK's annual reports, press releases, and circulars.

The interview guide comprised of three sections. The first part inquired about general information, the second part comprised of questions on competitiveness, and part three inquired on challenges of outsourcing.

3.4 Data Analysis

Data gathered from the interviews was analyzed using content analysis. This is a research method for the subjective interpretation of the content of text data through the systematic classification process of coding and identifying themes or patterns (Hsieh and Shannon, 2005). The data was qualitative in nature.

Content analysis is used to systematically summarize written, spoken, or visual communication in a quantitative way. The interview guide was edited for completeness and consistency, and the results were tabulated for ease of comparison and interpretation of the findings.

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

The research objective was to establish the achievement of competitive advantage through outsourcing at the National Bank of Kenya. This chapter presents the analysis and findings with regards to the objective and discussion of the same and is divided into three sections namely; respondents profile, the outsourcing strategies at the NBK and the challenges facing outsourcing strategies at the bank

4.2 Respondents Profile

This part of the interview guide was intended to assess the capacity of the respondents to answer the questions on the interview guide and also whether they were versed with the subject matter of the study. The respondents comprised the top and middle level managers of the bank namely; Deputy Managing Director, Client Relationship Manager, Information Technology Manager, Human Resource Manager, and the Administration Manager. These respondents were purposely selected by the researcher because they were deemed to be dealing in the company with issues relating to decisions relating to outsourcing of services and products. This represented 100% response rate.

All the respondents interviewed had university degrees with 3 of them having Masters Degrees. Their work experienced spans a total of 68 years in various departments within the organization and other firms in the banking industry. In addition, the views of both genders were represented in the interviewees because two of the respondents were female against three men. This meant that the views expressed by the respondents were not gender biased. With this background, the researcher felt that the respondents had the necessary expertise and experience on the research subject matter and will become invaluable to the realizable of research objective.

4.3 Outsourcing of services at the National Bank of Kenya

This section of the interview guide sought to establish from the respondents the nature of outsourcing being sought at NBK by various customers in the bank. From the results of this section, it will then facilitate the establishing of whether the same process has become a source of competitive advantage to the bank.

The researcher sought to establish from the respondents the reasons that encouraged the firm to become a preferred institution by clients to outsource services from. The interviewees noted that in the present day competitive environment that businesses operate in, it has become a competitiveness issue for the business units to outsource services and leaving them to concentrate in matters that they have a core competency on the same. The results to the question on why customers decide to outsource services from the bank was varied but centered the need to reduce cost of investment, reduce operating costs, reduce risk by transferring to third parties the same risk and also to enable the client concentrate on its core activities. According to Quinn and Hilmer (1994), a major strategic concept in outsourcing decisions is core competence. It was also pointed out that there is need for the organization to reduce risk exposure to changing technology and/or changing buyer preferences through reduction of the lead times of delivery of services and this can be achieved better if the services can be outsourced.

The common services that were found to be popular with being outsourced from the bank includes; cash collections from the clients offices and being disbursed to the various bodies such as Kenya Revenue Authority, NHIF, Kenya Airways, Kenya Power, Payroll processing, Credit card processing, School fees collection, Tax collection and credit card process. This means that most of the services that the bank has captured will be in the area of being an agent to most of these clients that source the services from the bank.

In the case of NBK, the respondents noted that a number of reasons can be pointed out to explain why the bank will be considered to be an appropriate institution to outsource the services from. The respondents noted that the cost charged for services by the bank is considered competitive considered to other players in the bank and they gave for example the cost of processing payroll to companies that the bank charges Ksh.125 per transaction while the next player in the market charges a minimum of Ksh.140 per transaction. This is considered to be cheaper from the customer's point of view. The development of a widespread and fast system that is efficient and faster by the bank makes it a preferred choice by customers.

The respondents noted that the bank has in the last five years invested in automation of its services to improve on the quality and speed of service to its customers. They for example noted that as a result of this automation, customers need to interact with the bank and source for the bank's services from their company's premises without necessarily visiting the bank's offices. It was also noted from the study that as a result of the bank investing in the automation of its services, the number of corporate clients has increased and new services being sought by clients. The respondents for example observed that the number of corporate clients seeking for outsourcing of services from the bank has increased from 1,245 in 2010 to a present number of 1,876 and this equally has led to the increase in the volume of transactions made per month. Some of the major corporate clients that the bank deals with at present include Kenya Revenue Authority, Higher Education Loans Board, National Housing Insurance Fund, Kenya Bureau of Standards, and various universities and colleges.

The study also sought to establish how NBK is utilizing outsourcing of services by various players to enhance its competitiveness. From the literature review, an outsourcing strategy creates a competitive advantage if three criteria are met. First, if implemented it must become a major or significant strength or capability of the organization. Second, it must be unique and proprietary to the organization. Third, the advantage provided by the outsourcing must be sustainable for at least three years. NBK was able to meet all the above criteria.

On this section a number of benefits were pointed out by the respondents to have arisen to the bank as a result of the bank going into agency services. The findings were that the bank has increased the penetration of its products to more customers as a result of accommodating clients who wish to source for the banks services. The respondents noted that majority of the recent clients pointed out were introduced to the bank's services from other clients and they in turn have introduced more customers. This was more so in the case of corporate clients who wished to process their payroll through the bank as well as school fees collection services. The Client Relationship manager pointed out that the segment of outsourcing has indeed increased the bank's profitability. On being asked how the outsourcing of services has influenced the bank's profits, the respondents noted that the organization profits margin has been affected positively. One of the respondents pointed out that as a result of undertaking an aggressive marketing of the services that can be outsourced in the bank, the monthly income from agency services has increased to Ksh 86M as compared to 56M that was registered one year ago.

The outsourcing of all services from the bank was noted to be automated and apart from the initial investment in the systems the operational cost to the bank is low. The respondents noted that outsourcing of licensing of driving license by KRA has brought in more clients who many of them have opted to open new accounts in the bank to facilitate the payment of the charges as well as make their remittances to KRA directly from their accounts in the bank. Costs for operating resources and investments of fixed infrastructure can be reduced step-by-step after the services have been outsourced and the payment to the contractor would convert the fixed costs into variable costs. They unanimously agreed that the decrease in labor and operating costs to the bank is based on a contractor's experience to perform or provide a certain service more efficiently and effectively

Asked if providing outsourcing was a feasible strategy in competing in the industry, the study respondents were overwhelmingly in agreement while stating that it depended on the volumes of services given and the uniqueness of the services provision compared to provision by its competitors, whereby high volume transaction would lead to high volume generation.

The undertaking of offering agency services to the clients was however noted to come with some risks. The interviewees noted that a number of risks faced the bank and this includes compensating the client as a result of lost transactions and monies, compensation as a result of failure to meet the terms agreed while signing the contract, risk of loss arising from fraud or theft by the bank employees and also the risk of the bank's system being hacked by outsiders. Several steps have been made to reduce the above risks. Some of the steps that the bank has taken include vetting all the staff to minimize incidences of negligence and fraud, strengthening internal controls systems and also strengthen the capacity of the ICT system to detect and alert of any abnormal commands.

4.4 Challenges of Outsourcing services

As one of the main objectives of this study, the researcher sought to find out what the respondents perceived were the challenges faced in providing outsourcing services. On this area, the respondents did note that the company's business outsourcing strategy matched with its overall company's strategy as the overall strategy is the basis for making business outsourcing choice. The company's overall strategy not only determines the business of home-made/outsourcing decisions, but also the outsourcing of the object, outsourcing model and supplier choices.

According to the findings, bringing up to date the systems which are compatible with the suppliers needs, pricing of services to break even with profit margins and customizing services for the various customers were among the challenges of outsourcing for the bank. On the other hand, a significant majority of the respondents were of the opinion that maintaining high and secure standards of service and being able to satisfy customer satisfaction and expectations within the specified and/or agreed period of time were additional challenges faced by the bank.

The nature of inputs required restricted the choice of outsourcing opportunities available to the bank. At times, it was noted that the bank will require a certain number of transactions per month to break even and serve the customers well. As a result, the interviewees pointed out that in some cases, the customers have tended to offer services that will involve a less number of transactions that become eventually uneconomical to the bank. The number of clients was also noted to change significantly especially the school fees transaction and that registers high transaction at the beginning of the new terms but fizzle out throughout the term until a beginning of a new term.

The other challenge that the bank faces in the course of offering the outsourcing of services include difference in the organizational cultures in which the rate of service sourcing and delivery might differ, ineffective communication mechanisms that may cause failure of outsourcing. Therefore, in order to handle these challenges, the bank has taken a number of initiatives to strengthen the management on the process of outsourcing. These measures include establishing a fully fledged department that handle the agency issues, having contracts with the outsourcing firms, incorporating service levels agreements in the contracts, regular inspection of subcontracted systems to assess their capacity, taking subcontractors through a validation process before being contracted, on-site inspections or verifications, conducting interviews for subcontractors drivers and purchase of insurance and inserting the tracking systems all the banks fleet of cash couriers.

4.5 Discussion of findings

This section links the findings to the theory and other studies that have been conducted in the past.

4.5.1 Comparison with theory

From the findings, NBK has achieved a competitive advantage through outsourcing over its competitors. Providing outsourcing was seen as a feasible strategy in the banking industry. According to Porter (1980), an outsourcing strategy creates a competitive advantage if three criteria are met. First if implemented it must become a major or significant strength or capability of the organization. Second, it must be unique and proprietary to the organization. Third, the advantage provided by the outsourcing must be sustainable for at least three years. NBK was able to meet all the above criteria.

National Bank of Kenya Limited embraced the Quinn and Hilmer (1994) model through its customers. The model suggests that activities with a high potential for competitive edge and a high degree of strategic vulnerability should be realized in-house. From the results a number of reasons were cited to explain why the bank was considered the most appropriate institution to provide outsourcing, and the main reason was that the cost charged for services was considered competitive in the market. Thus, according to Barney (1991), a competitive advanta[illegible] enables the firm to create superior value for its customers and superior profits for its [illegible]

A number of challenges were also pointed out from the [illegible]ings which [illegible] included bringing up to date the systems that are compatible with [illegible]e suppliers[illegible] pricing of services to break even with profit margins and customizing se[illegible] [illegible]ious [illegible] as customers. Bahli and Rivard (2003) noted that if firms only foc[illegible] term benefits of outsourcing without considering these challenges, they may fail to access orginal goals of outsourcing.

4.5.2 Comparison with other studies

In Kenya, several other studies have focused on strategic outsourcing. Wandabwa (2006), study on a survey of the current outsourcing practices by Commercial Banks n Kenya, found out that outsourcing is widely used in the banking sector and anaging outsourced business processes is the key to providing competitive services aso shift focus on core activities. It was noted from the study that as a result of BK investing in the automation of its services, the number of corporate clients had rased and new services were being sought by clients.

udy by PriceWaterhouseCoopers (1999), established that outsourcing had moved kedly from attending a single function more efficiently, to reconfiguring a whole ess in order to attain greater shareholder value across the enterprise. In effect, hasis is shifting from outsourcing parts, facilities and components towards ourcing the intellectual based systems. This is evident from the study as some of teps that NBK has taken include strengthening internal controls systems and also CT systems that detect and alert any abnormal commands.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter sets out to discuss the summary of the findings, draw conclusions, and make recommendations.

5.2 Summary of the findings

As one of the oldest banks in the country, National Bank of Kenya Limited has a wide branch network and with the contracting of agents to offer some of its services, the bank can be said to have a wide coverage in the country. However, the bank has in the recent past faced increased competition from other players in the banking sector that offer the same traditional banking services in which in some cases are not differentiated. This has led to a decline in the bank's revenue from the mainstream banking services.

In order to reverse this trend, the bank has taken a deliberate move to differentiate its services and utilize its resources to gain competitive advantage. One of the moves that the bank has taken to gain competitiveness is to offer outsourcing services to both public and private entities. The number of corporate clients that the bank serves has increased many folds and currently includes KRA, NSSF, NHIF, HELB and various educational institutions. The outsourcing services that the bank offers include cash collection, tax and school fees collection, payroll processing and also credit card processing. The result findings show that as a result of outsourcing, the bank has gained some level of competitiveness and also a competitive advantage over other players in the banking industry. The bank has gained good competitiveness such that it currently collects around 45% of all KRA remittances and with the high level of collection, it has been able to receive proportionately high commissions from the transactions. The other benefits that has accrued to the bank has a result of servicing outsourced services include an increased level of revenue, selling more banks products to new clients and the recruitment of additional customers to the bank.

The bank has however faced a number of challenges in the course of servicing the outsourced services. These challenges include the small number of transactions that a client might request which will be uneconomical to the bank since for the cost of processing to be covered, there should be a minimum number of outsourced transactions that a client should offer. In addition, there are some types of transactions that are not constantly sourced throughout the operating period and instead they are periodic. Such services as collecting of school fees however get compensated by the large volume of transactions that are involved. The other challenge that the bank faced in the course of offering the outsourcing services, include difference in the organizational cultures in which the rate of service sourcing and delivery might differ, ineffective communication mechanisms that may cause failure of outsourcing. Therefore, in order to handle these challenges, the bank has taken a number of initiatives to strengthen the management of the process of outsourcing.

5.3 Conclusions

From the above findings on the research questions, it can be concluded that outsourcing is a perfect tool for an organization to gain competitive advantage. Organizational competitive advantage can come about from the organization differentiating its products and services from the other players and also through offering services that meet the customers' expectations. It is also coming out that the small commissions that might result from the small number of transactions can generate competitiveness to a firm. It is also clear from the study that for effective success in the generation of a firm's competitiveness, the organization culture and an organization structure should be flexible enough to be able to identify fast enough opportunities arising and also to hasten the decision making process.

Another point that can be concluded from the study is that for service outsourcing to be successful, a firm should consider partnering with other smaller firms or agents to represent it in regions that it has no coverage limit. It is also clear from the research that outsourcing also provides a platform for revenue generation, client base expansion and profit Maximization Avenue. The researcher believes that if proper operational and control structures are put in place along with overcoming challenges and risks of outsourcing, provision of outsourcing services has the capacity to propel the banks ambition and vision to greater heights giving it an edge over its competitors.

In the course of implementing outsourced services, it is important that the firm involves all the stakeholders both internal and external in order for the organization to achieve the desired results. This means that decision making should be all inclusive to reduce the anticipated level of resistance in the process when it is being implemented.

5.4 Limitations of the Study

The study adopted a case study in which only one organization was studied. It would however be advisable if the study covered many other organizations in the same banking industry to validate the present findings with other organizations. In addition, the study interviewed only senior managers in the bank who were actually involved in the formulation of the outsourcing services in the bank and will probably give a more positive effect of the strategy and more economical on the weaknesses of the strategy.

5.5 Recommendations of the study for policy and practice

This study makes several recommendations for policy implementation and also suggestions for further research.

5.5 .1 Recommendations with policy Implication

Foremost, the study established that the bank's outsourcing strategies approach is top-down and this approach was found to exclude most of the staff in getting involved in such important exercise. As a result it is recommended that the organizational strategy should be all inclusive and preferably a bottom up approach be adopted and though it might be expensive, its cost benefit analysis will support the approach. What this means is that the process of outsourcing should be all inclusive to both internal and selected external stakeholders who will be affected by the outsourcing strategy.

Secondly, the study found out that the outsourcing strategy process is a time and resource consuming exercise. The process should therefore not be hurried much and firms should adopt the most economical procedure that offers less waiting time and a higher spatial convenience than traditional process and thus attractive to a large and quickly growing segment of customers. However, before making large-scale investments in a given process it is recommended that the relevant customer segments are identified and that attempts should be made to predict the development of their sizes.

5.5 .2 Recommendations for practice

NBK should implement variables that manifest Customer Service Management (CSM) to retain their customers, remain competitive and increase their market share. When outsourcing, banks should consult other stakeholders to minimize mistakes committed.

5.6 Suggestions for further research

The researcher conducted a case study at National Bank of Kenya Limited and recommended that a study should also be carried out to determine the effect of outsourcing on other banks in Kenya and/or East Africa.

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APPENDIX: Interview Guide

1. What is your job title?
2. How long have you worked for this company?
3. Describe and explain your knowledge and understanding of outsourcing?
4. What functions/ services are other organizations outsourcing from National Bank of Kenya?
5. How was the decision arrived at providing activities to outsource?
6. In your opinion, what are the reasons for outsourcing the bank's services?
7. How has the organization benefited from providing outsourcing?
8. How is National Bank of Kenya utilizing outsourcing strategy as a competitive tool?
9. Is providing outsourcing a feasible strategy in competing in the industry?
10. What are the challenges of providing outsourcing?
11. How have you been able to overcome them?
12. What are the foremost outsourcing risks National Bank of Kenya is concerned with?
13. How are they being addressed?

14. What are the strategic goals for providing outsourcing?

15. Has the organization's profit margin improved?

16. Are the customer's satisfied with the bank's services?

Note: All the written information is applicable only for the study. The participants are assured that the information they give is well-privatized prior to the security and ethical considerations.