

**A SURVEY ON STRATEGIC RISK MANAGEMENT
PRACTICES BY LARGE COMMERCIAL BANKS IN
KENYA**

NJERI VIOLET WANJIKU

**A MANAGEMENT RESEARCH PROJECT SUBMITTED IN PARTIAL
FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTER
OF BUSINESS ADMINISTRATION, SCHOOL OF BUSINESS, UNIVERSITY OF
NAIROBI**

SEPTEMBER 2010

DECLARATION

I declare that this is my original work and has not been submitted for award of a degree in any other university.

Signature.....

Date.....

Violet Wanjiku Njeri

D61/P/8893/2004

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

Signature.....

Date.....

Dr. Wahome Gakuru

Lecturer, University of Nairobi

DEDICATION

I dedicate this project to my dear mother Elizabeth for her love, guidance and encouragement throughout my education. My husband Kimani for his support, Daniella my lovely daughter for bearing with my tight schedule. May God bless you.

ACKNOWLEDGEMENT

First and foremost I thank God for giving me the strength to go through this demanding yet rewarding programme and above all for making this a reality.

Many thanks to my supervisor, Dr. Wahome Gakuru for his invaluable support and guidance during this project.

Special thanks to my family and siblings for their encouragement and confidence in me.

ABSTRACT

Every bank is faced with several types of risks key among them being strategic risk. In essence, a bank must accept certain levels of risk taking into consideration the risk reward trade off as risks cannot be totally avoided. The strategic risks faced by any bank may vary in degree depending on the size of the bank, business complexities, business volumes, system sophistication and capability.

Strategic risk is the current or prospective impact on earnings or capital arising from adverse business decisions, improper implementation of decisions or failure to respond to changes in the competitive environment, business cycles, customer preferences or product obsolescence. As such, strategic risk management is part of strategic management that entails positioning a firm within its environment (internal and external) to ensure continued success.

The research was a census survey on 13 large commercial banks in Kenya. The objectives of the study were to determine the strategic risk management practices adopted by large commercial banks and the challenges faced by these banks in their strategic risk management practices. The researcher established that there is an appreciable level of strategic risk management practice among the large commercial banks as exhibited by the findings. The study found out that banks have adopted strategic risk management practices and though there was a slight variance in approach between the banks, the most commonly adopted practice centered on strategic risk assessment, evaluation, monitoring, control and reporting. These strategic risk management practices are discussed in the ensuing sections in detail.

The researcher recommends that banks invest more in automated strategic risk management tools which would enhance analysis and profiling of their strategic risk. It would also be appropriate to appoint senior managers as the strategic risk champions.

Further study can be done on the relationship between corporate governance or strategic planning divisions and strategic risk management. Studies may also be done on the relationship between strategic risks and other risks in banks.

TABLE OF CONTENTS

PAGE NO.

Declaration.....	ii
Dedication.....	iii
Acknowledgement.....	iv
Abstract.....	v
List of tables.....	x
List of figures.....	xi
CHAPTER ONE: INTRODUCTION.....	1
1.1 Background of the Study.....	1
1.1.1 Concept of Strategic Risk Management.....	1
1.1.2 Banking in Kenya.....	3
1.1.3 Business Environmental Shocks.....	4
1.2 Statement of the Problem.....	5
1.3 Objectives of the study.....	6
1.4 Importance of the study.....	6
CHAPTER TWO: LITERATURE REVIEW.....	8
2.1 Strategic Risk Management Practice.....	8
2.2 Strategy and Risk.....	10
2.3 Strategic Risk Assessment.....	12
2.4 Strategic Risk Evaluation and Response.....	13
2.5 Strategic Risk Monitoring and Control	14
2.6 Objectives of Strategic Risk Management.....	15
2.7 Importance of Strategic Risk Management.....	15
2.8 Risk Appetite and Tolerance	16
2.9 Strategic Risk Management Framework and Policy.....	16

CHAPTER THREE: RESEARCH METHODOLOGY.....	18
3.1 Research Design.....	18
3.2 Population.....	18
3.3 Data Collection.....	18
3.4 Data Analysis.....	19
CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION.....	20
4.1 Introduction	20
4.2 Background Information on Banks Studied.....	20
4.2.1 Branch Network.....	20
4.2.2 Bank Ownership.....	21
4.2.3 Independence of Risk Departments.....	22
4.2.4 Usage of Risk Softwares.....	22
4.2.5 General Risk Management	23
4.3 Strategic Risk Management Information.....	24
4.3.1 Assessment and Evaluation.....	25
4.3.2 Monitoring, Reporting and Communication.....	27
4.3.3 Board Risk Committees.....	28
4.3.4 Strategic Risk Management Development.....	29
4.3.5 Types of Risks.....	30
4.3.6 Challenges in Strategic Risk Management.....	30
CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS...31	31
5.1 Introduction.....	31
5.2 Summary of findings	31
5.3 Limitations of the Study.....	32
5.4 Conclusion.....	33
5.5 Recommendations.....	33
5.6 Suggestion for Further Study.....	34

REFERENCES.....	34
APPENDICES	
Appendix 1: Large Commercial Banks.....	37
Appendix 2: Questionnaire.....	38

LIST OF TABLES

Table 1: Strategic Risks.....	11
Table 2: Risk Attitudes and Strategic Choice.....	12
Table 3: Bank Ownership.....	22
Table 4: Strategic Risk Identification Responsibility.....	25
Table 5: Strategic Risk Identification	26
Table 6: Board Risk Committee Composition.....	29

LIST OF FIGURES

Figure 1: Branch Network.....	21
Figure 2: Strategic Plan.....	23
Figure 3: Level of Communication.....	27

CHAPTER ONE: INTRODUCTION

1.1 Background of the study

Businesses face many risks that could present threats to their success, therefore risk management should be a central part of any business' strategic management. The recent global economic crisis shed light on the importance of sound risk management practices in banks. Thus, given that strategic risk management can largely contribute to the success of a bank, conducting this research based on the large banks which hold a large stake in the industry both in terms of deposits and advances was important. Bessis (2002) defines risk as the probability of an event and its consequences while risk management is the practice of using processes, methods and tools for managing these risks. According to the Institute of Risk Management (2007), risk management focuses on identifying what could go wrong, evaluating which risks should be dealt with and implementing strategies to deal with those risks. Businesses that have identified their risks are better prepared and have a more cost-effective way of dealing with them.

1.1.1 Concept of Strategic Risk Management

Strategic risk is the current or prospective impact on earnings or capital, arising from adverse business decisions, improper implementation of decisions or failure to respond to changes in the competitive environment, business cycles, customer preferences or product obsolescence (<http://www.centralbank.go.ke>).

Sadgrove (1996) further argues that strategic risk management is part of strategic

management that entails positioning a firm within its environment both internally and externally, to ensure continued success. An organization should therefore have policies on business strategy as they are critical in defining the business segments that the institution will focus on, both in the short and long run. Every bank is faced with several types of risks such as operational risk, credit risk, market risk, liquidity risk, foreign exchange risk, price risk, compliance risk, interest rate risk and strategic risk. In essence, a bank must accept certain levels of risk taking into consideration the risk reward trade off as risks cannot be totally avoided. The strategic risks faced by any bank may vary in degree depending on the size of the bank, business complexities, business volumes, system sophistication and capability (<http://www.centralbank.go.ke>). Abuya (2008) holds that the underlying premise of strategic risk management is that every entity, as it seeks to provide value for its stakeholders, faces uncertainty and the challenge for its management is to determine how much uncertainty to accept as it strives to grow stakeholder value.

Strategic risk management enables managers of an organization to effectively deal with uncertainty, associated risk and opportunity, thereby enhancing the capacity to build value. It encompasses aligning risk appetite and strategy, enhancing risk response decisions, reducing operational surprises and losses, identifying and managing multiple and cross-enterprise risks, seizing opportunities and improving deployment of capital (COSO, 2004).

The researcher therefore intended to investigate and document the existence of strategic risk management practices which would include existence or absence of clearly stipulated strategic risk management policies, processes and frameworks.

1.1.2 Banking in Kenya

Kippra (2009), holds that the banking sector portrays an oligopolistic market structure. The sector is still non competitive as only a few large commercial banks dominate the sector while majority are small. The five largest banks alone control over fifty percent of net advances, customer's deposits and total net assets in the industry.

According to Central Bank of Kenya (CBK), the banking industry has forty three licensed commercial banks and one mortgage company. These banks are categorized into three peer groups large, medium and small based on various parameters such as size of their asset base, advances portfolio, customer deposits, capital and profits (<http://www.centralbank.go.ke>). Out of the 43 banks, 13 are categorized as large banks and they dominate the market in terms of net assets, customer deposits, net advances, capital and profits. This research will be based on the large commercial banks only. The industry has been faced with a lot of dynamism such as issuance of prudential guidelines on risk management, business continuity management by the CBK, enactment of The Proceeds of Crime and Anti-Money Laundering Act, 2009 which calls for vigilance especially by bank officials on reporting of suspicious transactions, value capping which implies that cheques and electronic funds transfer settled through the automated clearing house will be done for amounts up to Kshs 1 Million only. Credit Reference Bureaus have also been licensed by CBK and these will facilitate sharing of credit information in the industry (<http://www.centralbank.go.ke>).

1.1.3 Business Environmental shocks

The banking industry in Kenya has been faced by various shocks in the recent past key among them being the post election violence, drought and global economic meltdown. The global economic downturn depressed Kenya's main export markets and this had an adverse impact on the banking industry given that it facilitates international trade and remittances. Similarly, the prolonged drought had a negative impact on the agricultural and power sectors. This adversely affected bank customers in those sectors as servicing of advances also proved challenging coupled with decreased business volumes (<http://www.africaneconomicoutlook.org>). On the other hand, the post election violence witnessed in various parts of Kenya raised pertinent questions on the resilience of the economy to sustain long periods of civil unrest and violence. The prolonged effects of the 2008 post-election violence depressed investor confidence and had adverse effects on the whole Kenyan economy and population (<http://www.fintradecapital.com>).

A recent survey by PWC Kenya revealed that CEOs are taking risk management more seriously following the recession. Forty-one percent of CEOs plan to make major changes to their company's approach to managing risk and another forty three percent report plans to make some change to their processes. Boards of Directors are also becoming more engaged in key aspects of management such as assessing strategic risk, monitoring financial health, and overseeing company strategy (<http://www.pwc.com>).

1.2 Statement of the Problem

CBK in its prudential guidelines clearly stipulates that the responsibility of managing strategic risks clearly rests with the Board of Directors while senior management of any bank have a responsibility to ensure there is an effective risk management process in place. In order to ensure an effective strategic risk management process, every bank should have a management information system that enables senior management to monitor current and forecasted economic conditions such as economic growth, inflation and foreign exchange trends. It is also important to monitor the strategic moves of peer banks so as not to be disadvantaged by lack of responsiveness to industry changes. Similarly, banks need strong internal control environments to ensure that they are not unduly exposed to strategic risks.

Various studies have been done on management of risks in banks especially credit risk, foreign exchange risk and interest rate risk in Kenya. Abuya (2008) studied Strategic Risk Management Practices with particular reference to state corporations in Kenya. His study focused on awareness and challenges that state corporations face in their strategic risk management practices. Andersen and Schroder (2010) hold that previous surveys on risk management practices show a similar pattern that risks are managed in silos focusing on financial risks and environmental hazards. Contemporary risk management practices tend to focus more on financial risks. Other studies carried out established that banks tend to concentrate more on other risk categories and overlook strategic risk. As such, strategic risk management practices have not been embraced as a modern management discipline owing to lack of commitment from top management.

This has led scholars to developing interest in this field as no study of holistic strategic risk management in banks has been carried out.

This study seeks to bridge the gap by establishing the strategic risk management practices by large commercial banks in Kenya. It will be guided by two questions mainly what strategic risk management practices are adopted by large commercial banks in Kenya and what are the challenges faced by large commercial banks in their strategic risk management practices?

1.3 Objectives of the study

- a) To determine the strategic risk management practices adopted by large commercial banks.
- b) To establish challenges faced by large commercial banks in their strategic risk management practices.

1.4 Importance of the study

This study will enlighten commercial banks on how to improve on their strategic risk management practices. The findings are expected to enable senior bank managers to manage current or emerging strategic risks and prepare for the future, develop tools and mitigation strategies for strategic risks. This will be based on the assumption that it is possible to prepare for major future risks and manage both current and emerging risks, and that it is possible to turn strategic risks into opportunities.

The research will also provide valuable information regarding strategic risk management in the banking industry. As upcoming managers the academicians will be furnished with relevant strategic risk management information. It will contribute to the general body of knowledge and form a basis of further research.

CHAPTER TWO: LITERATURE REVIEW

2.1 Strategic Risk Management Practice

Evolution of risk management practice is traced back to the mid-1970s, evolving from the older field of insurance management. The term was adopted because the new field had a much wider focus than simply insurance management. Risk management includes activities and responsibilities out-side of the general insurance domain. Insurance management focused on protecting companies from natural disasters and basic kinds of exposures such as fire, theft, and employee injuries. Risk management on the other hand focused on these kinds of risks as well as other kinds of costly losses emanating from risk exposures. In the 1980s and 1990s, risk management grew into being a vital part of an organization's planning and strategy thereby becoming integrated with more and more organizational functions as the field evolved. The scope of risk management practice has increased to encompass large-scale, organization-wide programs, thereby being commonly known as Enterprise Risk Management (<http://www.referenceforbusiness.com>).

COSO (2004) defines Enterprise Risk Management as

A process effected by an entity's board of directors, management and other personnel, applied in strategy setting across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.

Emerging trends on risk management practice have been noted over time. In the 1990s, new areas of risk management began to emerge and these provided managers with more options to protect their companies against new kinds of exposures. Risk managers started assessing environmental risks such as those arising from pollution, waste management, and environmental liability to help make their companies more profitable and competitive. Further, tighter environmental regulations also caused businesses to have risk managers check their compliance with environmental policies to prevent possible penalties for non compliance.

Generally, strategic risk management practice concerns the management of events that cannot be predicted. The contemplated events usually are adverse but it is not this feature that makes strategic risk management an interesting subject rather it is the quality of unpredictability in the events contemplated. This quality calls for a particular decision framework (Doherty, 1985). The Institute of Risk Management (2007) holds that the process of 'top-down' management of risks faced by a company has been variously labelled and defined as business risk management, holistic risk management, strategic risk management or enterprise risk management. The underlying sense of all these terms is that somebody looks at what the organization is trying to do in terms of its objectives, what opportunities it has and the things that threaten its ability to grasp those opportunities. This includes the process of planning, organizing, leading and controlling activities of the organization to optimize the potential impacts of risk on earnings, assets and capital. Risk is thus associated with opportunities which is sometimes called upside risk and threats also known as downside risk. The latter often dominates the risk agenda

and contributes to a rather negative reaction of many organizations to the process of strategic risk management. An approach that recognizes that taking upside risk is the very process that drives innovation and the pursuit of new markets while offering techniques to keep the potential exposure proportionate is more likely to find favour with organizations.

2.2 Strategy and Risk

According to Sadgrove (1996), strategic risks are the issues which require companies to think on a grand scale. These risks should be tackled at board level and require strategic planning. Given that strategy and risk go hand in hand, organizations operate in an increasingly changing regulated world and plans need to be forecast. Customers also occasion strategic risk given that their changing attitudes and expectations make them less predictable. Competition on the other hand is also a strategic risk both globally and locally. New technology also brings new threats and opportunities which if ignored can occasion new competition. Strategic risk may therefore also arise from formulation of strategic plans, business plans, the implementation of plans that are inappropriate and inconsistent with internal and external factors. In its prudential guidelines, CBK further points out that strategic risk is a function of the compatibility of an organization's strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals and the quality of implementation.

Table 1: Strategic Risks

Strategic Risks	Have an impact on the company's	Solutions can be found in
Government and economic factors	Costs	Strategic Planning of markets and products Empowerment
Customers	Prices	Quality engagement
Competitors	Products	Customer care
New technology	Sales	Investment Innovation Cost Reduction

Source: The Complete Guide to Business Risk Management, 1996

In the past, managing risk was done in a fragmented manner within functions or business units. As a result of this fragmented approaches, companies would take huge risks in some areas of business while over managing substantially smaller risks in other areas. Realization of this has since led to adoption of Enterprise Risk Management which is a corporatewide, integrated process for managing uncertainties that could negatively or positively influence the achievement of a corporation's objectives. Enterprise Risk Management is being adopted because of the increasing amount of environmental uncertainty that can affect the entire corporation (Wheelen and Hunger, 2008).

The attractiveness of a particular strategic alternative is more often than not a function of the risk it entails. Risk therefore is comprised not only of the probability that the strategy will be effective but also of the amount of assets the organization must allocate to that strategy and the length of time the assets will be available for other uses. Top management's perception of risk helps understand the potential acceptability of a given organization's strategic option. Insofar as they influence managerial attitudes, the risk attitudes of managers and stakeholders will eliminate some strategic alternatives and highlight others (Bessis, 2002).

Table 2: Risk Attitudes and Strategic Choice

Managerial Attitude towards risk	Probable choice filters	Probable Strategies
Risk is necessary for success. Optimistic; high risk leads to reward	High risk projects are acceptable or desirable	Expansion
Risk is a fact of life and some risk is acceptable	Balance high risk choices with low risk choices (bet hedging)	Combination
High risk is what destroys enterprises; it needs to be minimized	Risk aversion: risky projects are rejected	Stability

Source: Business Policy and Strategic Management, 1988

2.3 Strategic Risk Assessment

This is the process of identifying each type of risk and its source. It entails a detailed

analysis of the risk that culminates in risk identification, determining the nature and source, how the risk can be measured either qualitatively or quantitatively, the probability of occurrence and impact of the risk if it crystallized. Strategic risk assessment may further entail developing risk registers, risk mapping alongside both quantitative and qualitative analysis of the exposures (Hertz and Thomas, 1983).

According to Judson (1996), failure to come to grips with risk analysis can undermine the execution of strategies in an organization. He further adds that carrying out risk assessment is imperative in tracking the implementation of any strategy. The greater the conflict of a strategy with the existing culture, the higher the strategic risk. However, if overall management competency is high and the organization is more responsive to the strategy, then the strategic risk is significantly reduced. Risk analysis clearly needs both organizational commitment and a sound structure for effective implementation. Strategic risk analysis can help formulate strategies which will typically be understood and implemented (Hertz and Thomas, 1983).

2.4 Strategic Risk Evaluation and Response

According to Andersen and Terp (2006), strategic risk evaluation refers to the process whereby a decision is arrived at about the significance of risks to the bank and whether the risks should be accepted, treated or responded to. It entails stipulating the probability of occurrence and the impact on occurrence. This then aids the process of mapping the identified scenarios based on estimated frequencies and severities occasioning a ranking and selection of the most significant risks for further treatment. Risk Response on the

other hand could be in terms of reducing the frequency of occurrence, severity of impact or making arrangements to finance the consequences of risk. It entails development of risk mitigation strategies and action plans which need to be included in the overall business plans of the organization to ensure successful implementation (Kogan, 2007).

Hillson (1999) suggests that risk response may adopt approaches such as risk avoidance which entails completely eliminating the exposure to a particular risk by reducing the risk to zero. Practically this does not work and is rarely a feasible solution since the only way to avoid all exposures to a particular risk is not to conduct any business activities associated with that risk. Risk transfer is another approach whereby the risk is passed over to a third party by insuring or outsourcing of critical services. Similarly, risk mitigation may be adopted as a response strategy where management may seek to reduce the probability of occurrence or impact of an adverse risk event. Finally, risk acceptance which entails planning for ways in which to deal with an event if it occurs may also be employed as a response strategy.

2.5 Strategic Risk Monitoring and Control

A bank should have a system that facilitates reporting of risks internally especially to senior management and the board of directors. It is also important to continuously monitor strategic risks. This helps ensure adherence to, effectiveness and relevance of policies and procedures relating to risk management. Reporting and communication entails preparing reports on a bank's risk profile and changes therein for the various stakeholders both internal i.e. the board and top management or external i.e. Central Bank, shareholders and customers.

2.6 Objectives of Strategic Risk Management

Andersen and Terp (2006) hold that there are various objectives of strategic risk management such as creating transparency which helps ensure that top management, the board of directors, the stakeholders and potential investors can evaluate the organization's significant exposures and appraise how they are dealt with by the organization. Enhancing risk awareness through creating an organizational culture is another objective whereby risk awareness becomes an integral part of all management decisions. It is important to control the risk environment by minimizing the probability of future losses and focusing on the risk appetite by maximizing the probability of success and minimizing the risk of not achieving organizational goals.

2.7 Importance of Strategic Risk Management

Sound strategic risk management is critical for every bank and this offers several benefits. The greatest benefit of managing strategic risk is that it helps in achievement of a bank's strategic objectives. Abuya (2008) holds that other reported benefits include better focus on business priorities, strengthening of the planning process and the means to help management identify opportunities. According to Andersen and Terp (2006), risk management helps create transparency, enhance risk awareness and provide a risk control environment.

2.8 Risk Appetite and Tolerance

According to Sagrove (1996), risk appetite refers to the level of risk an organization is prepared to be exposed to before it decides the necessary action to take. By setting a risk appetite, the organization is able to allocate appropriate resources. Setting the risk appetite has various advantages such as helping the organization to clearly measure and compare its risks considering the potential losses and gains. It also helps to see if resources are wasted on risks and to ascertain whether organizations recognize that attention should be focused on risks above the defined level. Other advantages include ensuring that objectives are set in line with the stipulated risk appetite and prioritizing the allocation of limited resources. If a risk falls outside the risk appetite threshold, risk management treatments and business controls are required to bring the exposure level back within the accepted range. Risk appetite may in certain circumstances be specified by law for example for health and safety. Risk tolerance on the other hand refers to the acceptable levels of variation relative to achievement of objectives. Defining the risk tolerance provides management with the assurance that the bank remains within its risk appetite which in turn provides comfort that the bank will achieve its objectives. The risk tolerance of a bank should be stipulated in the respective policies within the bank (Bessis, 2002).

2.9 Strategic Risk Management Framework and Policy

Risk Management Prudential Guidelines issued by the CBK stipulate that policies on business strategy are critical in defining the business segments that a bank will focus on,

both in the short and long run. There should be clear guidelines on the frequency and procedure for reviewing a bank's business strategy. In order to ensure an effective strategic risk management process, every institution should deploy a management information system that enables management to monitor current and forecasted economic conditions such as economic growth, inflation and foreign exchange trends. Institutions also need strong internal control systems to ensure that they are not unduly exposed to strategic risks (<http://www.centralbank.go.ke>).

CBK prudential guidelines further stipulate that strategic risk management should be based on an established Strategic Risk Management Policy, which is in compliance with the institution's overall policy of risk management. The policy should provide general guidelines to strategic risk management such as definition of strategic risk, sources of strategic risk both internal and external, risk mitigation factors and a bank's accepted tolerance for strategic risk exposure.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Research Design

The research design constitutes the blueprint for collection, measurement, and analysis of data. This entails design arrangements of conditions for collection and analysis of data in a pattern that aims at being relevant to the research. It is a conceptual structure within which a study is conducted (Kothari, 2004).

This study was a census survey where responses were sought from respondents in all the thirteen large commercial banks in Kenya. It was descriptive in nature and answers to the research questions were obtained using questionnaires. This design was preferred because it was best suited to describe existing practices. Significant best practice variables were used to conduct the study which helped answer the research questions. The study results formed the basis for making conclusions.

3.2 Population

The population of this study was the thirteen large commercial banks in Kenya as categorized by the Central Bank of Kenya and a census survey was conducted. They were expected to provide information on their strategic risk management practices.

3.3 Data Collection

The data collection was qualitative in nature, intended on answering 'what' and 'how' questions. Being a qualitative research, it was expected to be an interpretative and subjective exercise. The data collection procedure used entailed administering questionnaires by physically visiting the banks and through electronic mail.

Questionnaires sent via e-mail were self administered. According to Saunders (2000), self administered questionnaires are usually delivered to and returned by respondents electronically.

Primary data was collected using questionnaires whereas secondary data was obtained from banks' annual reports and financial experts reports.

The main target respondents in the banks were chief risk officers, senior bank managers or heads of strategic and corporate planning divisions. The questionnaires were then picked from the physical locations or emailed back to the researcher. After the questionnaire sheets were collected and secondary data obtained from bank's annual reports and financial experts reports, analysis was done for conclusion of the study.

3.4 Data Analysis

Data collected from the primary and secondary sources was summarized and analyzed in order to derive meaning out of it. Data analysis involved a number of closely related operations that were performed with the aim of deriving conclusions that would address the research questions. This was accomplished using tables, charts, percentages, ratios and other qualitative techniques.

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the findings and analysis of data collected on strategic risk management practices by large commercial banks in Kenya. From the study population target of 13 respondents, the response rate was eighty five percent. The 11 respondents constituted 5 risk managers and 6 risk officers. This implies that the responses were given by well informed respondents doing the actual risk management jobs in the large commercial banks.

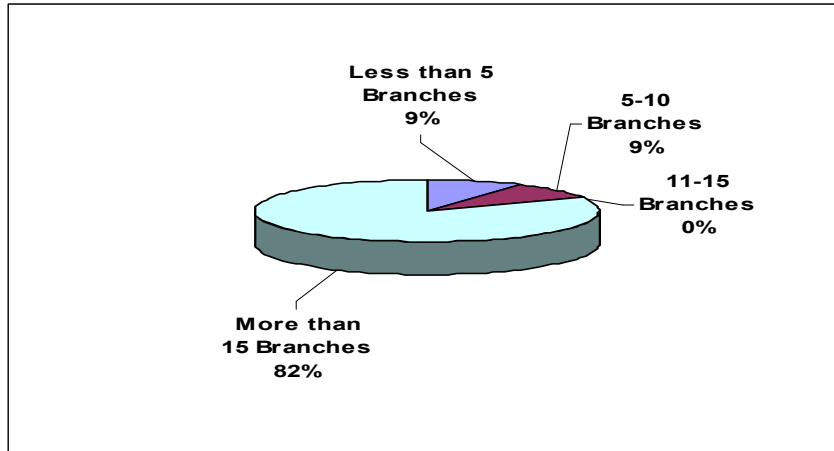
4.2 Background Information of the Banks Studied

The researcher administered a questionnaire that sought to collect general information about the banks in one section and specific strategic risk management practice data in another section. Data on background information collected is analysed below.

4.2.1 Branch Network

The study sought to establish the branch network of large commercial banks and eighty two percent of respondents had over 15 branches in their banks. Nine percent had between 5 – 10 branches whereas the other Nine percent had less than five branches. This is represented in Figure 1

Figure 1: Branch Network



This shows that most of the large commercial banks have a wide branch network, further reinforcing the need for sound strategic risk management practices given that branch expansion is part of strategy. Opening branches in localities that do not rhyme with a bank’s target market may pose grave strategic risks to the bank.

4.2.2 Bank Ownership

Responses on bank ownership are summarized in Table 3

Table 3: Bank Ownership

Ownership	No. of Banks	Percentage
Local	5	45%
Government	0	0%
Foreign	4	36%
Local & Foreign	2	18%
Total	11	100%

Banks with either full or partial foreign ownership constitute about fifty four percent of the respondents. This informs the researcher that the strategic systems and structures of these banks may be highly influenced by those of the parent companies.

4.2.3 Independence of Risk Departments

All respondents responded positively when asked if their banks have independent risk departments. This means that each of these banks has a dedicated team reviewing their bank's risk profile. It indicates that all the banks are in compliance with the central bank requirement. Setting up of independent risk departments is further justified by the sizes of these banks.

4.2.4 Usage of Risk Softwares

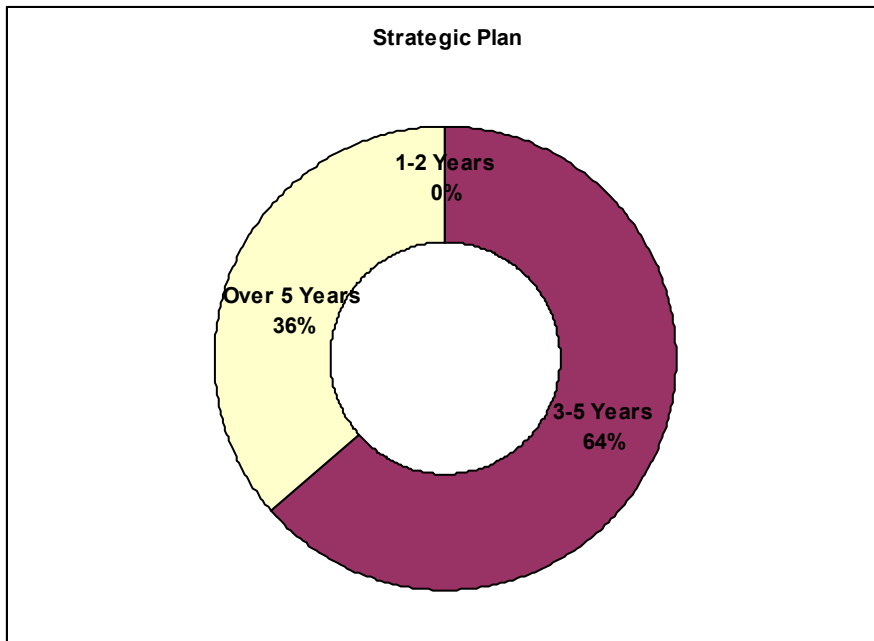
The ratio of banks using risk softwares and banks not using risk softwares was 6:5 which is quite fair. However, this implies that a considerable number of banks are still relying on manual intervention in risk management. This means that the risk management being carried out by such banks could be quite basic given that sophisticated risk management requires software intervention.

4.2.5 General Risk Management

Fifty five percent of the respondents indicated that their risk departments were monitoring operational, credit, market, interest rate, compliance, strategic, liquidity and foreign exchange risks. Forty five percent indicated that they monitored some of these risks. This is a clear indication that most of the banks have adopted a centralised approach to risk management.

There was a one hundred percent positive response rate on existence of strategic plans for all the banks. The period covered by these strategic plans varied slightly as indicated in Figure 2

Figure 2: Strategic Plan



The ratio of banks which set aside budgetary allocations to fund risk management activities against banks that don't was 9:2 respectively. This shows that management of most large commercial banks appreciate the need to fund risk management activities.

On having formally approved risk policies, one hundred percent of the respondents indicated that their banks have these in place while ninety one percent further indicated that the policies are approved by the board. Nine percent of the respondents indicated that their risk policy is approved by the risk committee. This implies that risk management has buy in from most of the banks' boards of directors and is accorded the attention it deserves just like any other function in the bank.

4.3 Strategic Risk Management Information

The researcher sought to gather data on specific strategic risk management practices from the respondents to gauge the level of appreciation for the need to manage strategic risks and the level of sophistication in managing the same. To this end, the researcher also sought to know if respondents believe that their current strategic risk management practices support achievement of their banks' objectives. One hundred percent of the respondents agreed that their strategic risk management practices support their strategic objectives. It shows that there is extensive awareness on the importance of strategic risk management in relation to the success of banks.

4.3.1 Assessment and Evaluation

Seventy three percent of the responses elicited that banks conduct risk identification during strategic planning whereas twenty seven percent elicited that they do not carry out this exercise during strategic planning. This shows that twenty seven percent of the large commercial banks forego an opportunity to identify risks during their strategic planning process thereby missing out especially on emerging strategic risks.

Responses on who is responsible for identification of strategic risks are summarised in Table 4.

Table 4: Strategic Risk Identification Responsibility

Responsibility	No. of Responses	Percentage
CEO	2	13%
Board/Executive Management	5	31%
Risk Manager	5	31%
Line Managers	3	19%
All Staff	1	6%
Others	0	0%
Total Responses	16	100%

All the 11 respondents agreed that their banks' management clearly understand that both the banks and their subsidiaries are exposed to strategic risks. This is a clear indicator of the awareness of exposure to strategic risks across the large commercial banks.

On the other hand, fifty five percent of the respondents indicated that their banks have strategic risk registers while forty five percent indicated that they do not have. It is important to have an inventory of risks as this would help the banks in profiling their risks.

The ratio of banks whose management recognize the significance of self assessments, ensure implementation and report the same to those which don't was 6:5 respectively. This is a welcome trend in strategic risk management given that the people doing the actual job are in a better position to assess their risk exposures and effectiveness of controls for the same.

Table 5 further summarizes responses on how banks identify their strategic risks.

Table 5: Strategic Risk Identification

Criteria	Yes	No
What can happen	11	0
How and why these risks arise	11	0
Source of the risk	11	0
Level of impact on crystallization	11	0

The one hundred percent positive response rate implies that banks are managing strategic risk more proactively. This is commendable as it involves envisaging what could go wrong in the foreseen future and mitigating the risks.

Responses were also sought from respondents on the criteria used by their banks to assess the impact of risks. All the respondents implied that their banks analysed risks based on their likelihood of occurrence and impact on occurrence. Eighty two percent further indicated that their banks assessed risks based on their financial, regulatory and reputation impact. Nine percent indicated that their assessment is based only on financial and regulatory impact whereas the other nine percent based their assessment on regulatory impact only. This implies that few of the banks may not be comprehensively assessing the impact of their strategic risks.

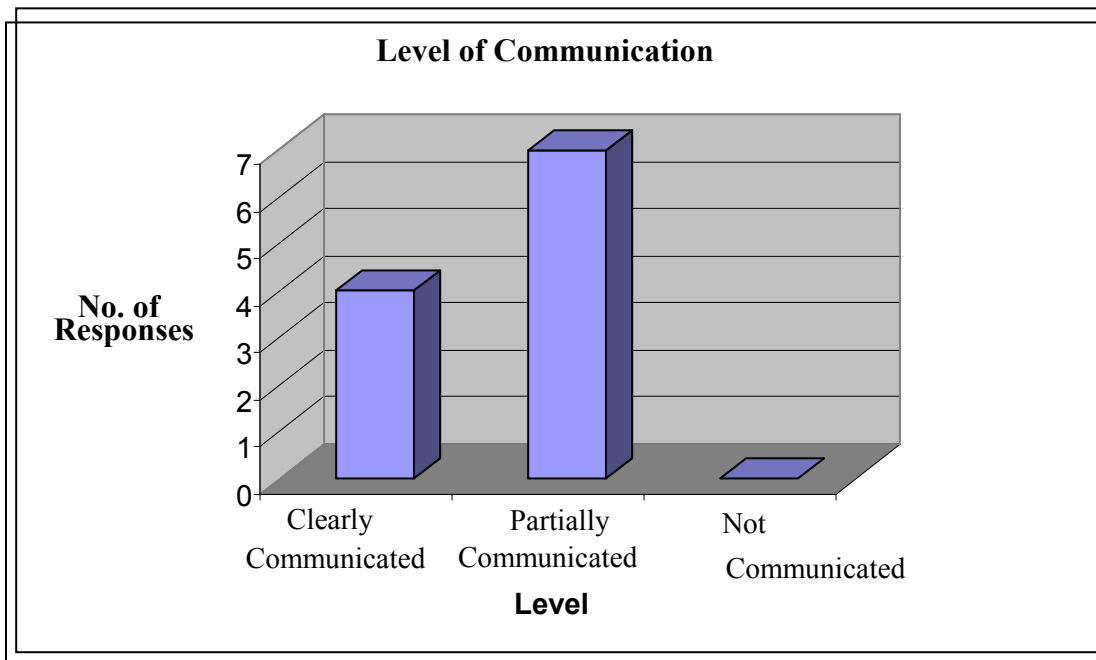
One hundred percent of the respondents elicited that their banks formally evaluate the existing controls and cost of controls. This is of high importance given that sometimes the cost of controls may be too high or the existing control may become obsolete over time.

4.3.2 Monitoring, Reporting and Communication

The ratio of banks that have strategic risk treatment plans to those without was 9:2 respectively. This shows that majority of the banks understand how to deal with the risks they are exposed to.

Responses on the level of communication and understanding of strategic objectives are summarised in Figure 3.

Figure 3: Level of Communication



Most of the banks management don't seem to be properly communicating the strategic objectives of their banks. It is important to communicate effectively as this helps in reduction of exposure to strategic risks especially when bank staff work in sync to achieve the same. Further, the ratio of banks that train their managers on strategic risk

management to those that don't was 8:3. On the other hand, the ratio of banks that have integrated risk management into their culture to those that haven't was 7:4. All these clearly show that there is a heightened level of communication on strategic risks in most of the banks and this is a good indicator.

Sixty four percent of responses revealed that banks have developed strategic risk management reports which they use to monitor risks whereas thirty six percent have not. On the other hand, while seventy three percent of respondents indicated that their banks measure and monitor risks using key risk indicators, board oversight and risk management programs by internal audit, eighteen percent rely on key risk indicators only, while nine percent rely on risk management programs by internal audit .

Secondary data analysed revealed that whereas most banks report on their management policies on risks such as operational, credit, market, liquidity, interest rate and foreign exchange risks, they hardly give any highlights on their strategic risk management policies.

4.3.3 Board Risk Committees

One hundred percent of the respondents indicated that their banks have board risk committees. However, whereas 10 respondents indicated that their board risk committees are not combined with the board audit committee, 1 respondent indicated that the two are combined. This is a good indication of a desirable level of independence in the strategic risk management of these banks.

Table 6 summarises responses on composition of the board risk committees for the various banks.

Table 6: Board Risk Committee Composition

Board Risk Committee Members	No. of Responses
Non Executive Directors	11
Independent Directors	8
Chair of the Board	6
Chief Risk Officer	11
CEO	9

10 responses elicited that the board risk committee is chaired by an independent non-executive director whereas 1 response elicited that the board chairman chairs the risk committee. On the other hand, ninety one percent of the respondents indicated that their board risk committees meet on a quarterly basis to review the banks risk profile while nine percent indicated that they meet on a monthly basis.

4.3.4 Strategic Risk Management Development

Eighteen percent of respondents felt that their banks' strategic risk management development was under best practice, thirty six percent well developed, twenty seven percent reasonably well developed while nineteen percent felt that it was quite basic. This informs the researcher that there is a lot of improvement required in strategic risk management in order to boost the confidence of banks and raise the standards to industry best practice.

4.3.5 Types of Strategic Risks

Respondents pointed out several strategic risks facing their banks such as reputational risk, failure to adhere to strategic plans, poor implementation of strategy, high staff

turnover, unclear strategic objectives, stiff competition, failure by top management to effectively lead banks in achieving their strategic objectives, technological risks, project failure, lack of long term sustainable investment climate and sudden change in sovereign laws especially for banks with some foreign ownership.

4.3.6 Challenges in Strategic Risk Management

Respondents pointed out the challenges they face in managing strategic risks such as inadequate competitor and industry information resulting in using unrealistic underlying assumptions when carrying out strategic planning, lack of appreciation of risk management fundamentals by stakeholders, lack of automated tools , lack of effective monitoring tools, lack of specially trained personnel, unclear guidelines on specific measurement of risks by the central bank, lack of synergy between corporate governance or corporate strategic planning divisions and risk management divisions.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary, conclusions and recommendations drawn from the findings of the study analyzed in the preceding chapter. The chapter is thus outlined into summary of the findings, limitations of the study, conclusion, recommendations, and suggestions for further research.

5.2 Summary of findings

Banks are faced with various strategic risks which necessitates proactive strategic risk management. Strategic risks identified by the study included poor or failed strategy implementation emanating from poor leadership by top management in achieving the objectives and lack of a sustainable investment climate as market forces get more dynamic.

The researcher established that there is an appreciable level of strategic risk management practice among the large commercial banks as exhibited by the findings. The study found out that banks have adopted strategic risk management practices and though there was a slight variance in approach between the banks, the most commonly adopted practice centered on strategic risk assessment, evaluation, monitoring, control and reporting. The banks have further defined frameworks for strategic risk management.

The study also established that banks with foreign ownership either fully or partially have

risk softwares and more defined risk structures which help enhance their strategic risk management practice. The researcher attributes this to the development of the parent companies from which they adopt certain practices. Further, the same banks with some foreign ownership exhibited a higher level of development in strategic risk management whereas local banks still need to enhance their strategic risk management to be at a reasonably well developed level. Findings of the study also indicated that banks have not adequately documented their risk appetite and tolerance levels. In order to maintain independence of strategic risk management and ensure ownership from top management, banks have set up board risk committees.

Findings of the study further show that large commercial banks are faced with several challenges in their strategic risk management. These include lack of specially trained personnel, lack of strategic risk management automated tools, low appreciation of strategic risk fundamentals by stakeholders, unclear guidelines from the central bank and lack of synergy between key divisions such as corporate governance and strategic risk management.

5.3 Limitations of the study

This study was coupled with a few limitations. Time was a great constraint as well as availability of senior bank managers. The time limitation was overcome through electronic exchange of the questionnaires and responses which helped reduce the turn around time. Despite not being able to access the senior managers in banks, the researcher managed to get heads of risk departments and risk officers who are equally well informed on their banks' strategic risk management practice.

5.4 Conclusion

Effective strategic risk management is crucial in banks and contributes to the success of a bank. This study has established existence of strategic risk management practices by large commercial banks in Kenya. Similarly, specialized training for practitioners has been identified as a key challenge. There is need for a professional body of strategic risk practitioners who can train experts who will in turn streamline strategic risk management in banks. This will help ensure that the level of appreciation for strategic risk fundamentals is heightened. Lack of training leaves a gap even in the boards of directors and senior management who should ideally driving the strategic risk initiatives owing to their level of decision making. The strategic risk management practices identified by this study would be further reinforced by proper training and automation of strategic risk management processes.

5.5 Recommendations

The researcher recommends that banks invest in automated strategic risk management tools as this will help in analysis and profiling of their risks. There is need for risk practitioners in the industry to come together and form a professional body either local or affiliated to international bodies. This will help foster experts and define industry best practice. Banks need to accord strategic risk management more attention and resources as this is a key area that greatly influences the success of banks and achievement of their strategic objectives. Senior bank managers should be the appointed strategic risk champions for the banks because strategies are set at that high level. Top level self

assessments should be embraced by banks as this would help ensure that their strategic risk levels are kept in check.

5.6 Suggestion for further study

Further study can be done on the relationship between corporate governance or strategic planning divisions and strategic risk management. Studies may also be done on the relationship between strategic risks and other risks in banks.

REFERENCES

- Abuya D, (2008). *Strategic Risk Management Practices Among State Corporations in Kenya*. Unpublished MBA Thesis. University of Nairobi
- Andersen, K. & Terp, A. (2006). *Risk Management*. In T.J. Andersen *Perspectives on Strategic Risk Management* .Copenhagen Business School Press, 27-45
- Andersen, T, J & Schroder, P.W. (2010). *Strategic Risk Management Practice. How to deal effectively with major corporate exposures*. New York: Cambridge University Press
- Barclays Bank of Kenya Ltd. *Annual Report 2009*
- Bessis, J. (2002). *Risk Management in Banking*. (2nd ed.).England: John Wiley & Sons
- CBK Newsletter*. Retrieved from:
<http://www.centralbank.go.ke/downloads/Market-News-Letter/>
- CEO Survey 2010. Retrieved from <http://www.pwc.com>
- COSO. (2004). *Enterprise Risk Management – Integrated 5th Edition*
- Doherty, N.A. (1985) *Corporate Risk Management; A Financial Exposition*, 10
- Dyer & Blair Investment Bank. (2008). *Banking Sector Report*.
- Enterprise Risk Management - Integrated Framework. Executive Summary* Retrieved From: http://www.coso.org/Publications/ERM/COSO_ERM_ExecutiveSummary
- Henriksen, P., & Uhlenfeldt, T. (2006). *Risk Management*. In T.J. Andersen (Ed.) *Perspectives on Strategic Risk Management*. Copenhagen Business School Press, 112.

- Hertz, D.B. & Thomas, H. (1983) *Risk Analysis and its Applications*, 316.
- Hillson, D (1999). *Developing Effective Risk Responses*. Proceedings of the Project Management Institute Annual Seminars & Symposium. Retrieved from:
<http://www.propernet.com>
- I&M Bank. *Report and Consolidated Financial Statements 2009*.
- Institute of Risk Management (2007). *Managing Business Risk; A practical guide to protecting your business* (J. Reuvid Ed.). London: Kogan Page Ltd
- Jauch, L.R. & Glueck, W.F. (1988). *Business Policy and Strategic Management*. (5th ed.). New York: McGraw-Hill, Inc
- Judson, A.S. (1996). *Making Strategy Happen: Transforming Plans into Reality*. (2nd ed.). Massachusetts: Blackwell Publishers Inc.
- Koch, T.W., & Macdonald, S.S. (2003). *Bank Management*. New Delhi: Timothy India Eastern Press
- Kothari, C.R. (2004). *Research Methodology – Methods and Techniques*, 33-55
- Pearce, J.A & Robinson, R.B. (2007). *Strategic Management. Formulation, Implementation, and Control*. (10th ed.). Boston: McGrawhill
- Risk Management*. Retrieved from
<http://www.referenceforbusiness.com/management/Pr-Sa/Risk-Management.html>

Sadgrove, K. (1996). *The Complete Guide to Business Risk Management*. Gower Publishing Ltd Vermont, 15

Saunders, M., Lewis, P., & Thornhill, A. (2000). *Research Methods for Business Students*. (2nd ed.). England: Pearson Education.

Sengupta, N., & Chandan, J.S. (2003). *Strategic Management. Contemporary Concepts and Cases*. New Delhi: Vision Books Pvt

The Chartered Institute of Bankers (1988). *The Bank's and Risk Management*. Cambridge Seminar

The Kenya Economic Report (2009). Retrieved from: <http://www.kippra.org/>

Wheelens, T. L. & Hunger, J. D. (2008). *Strategic Management and Business Policy, Concepts and Cases*. (11th Edition). New Jersey: Pearson Education Inc.

Websites

www.africaneconomicoutlook.org

www.fintradecapital.com

APPENDICES

APPENDIX 1: LARGE COMMERCIAL BANKS IN KENYA

1. Bank of Baroda
2. Barclays Bank
3. CFC Stanbic Bank
4. Citi Bank
5. Commercial Bank of Africa
6. Co-operative Bank of Kenya
7. Diamond Trust Bank
8. Equity Bank
9. I&M Bank
10. Kenya Commercial Bank
11. National Bank of Kenya
12. NIC Bank
13. Standard Chartered Bank

APPENDIX 2: QUESTIONNAIRE

This questionnaire has been prepared in relation to the objectives of this study. It seeks to establish strategic risk management practices by large commercial banks in Kenya. The information provided in the questionnaire will only be used for academic purposes and will be treated with utmost confidentiality.

The questionnaire is in two parts, A and B

Part A consists of questions aimed at obtaining general information about your organization.

Part B seeks information on the strategic risk management practices of your organization

Section A: General Information

1. What is the name of your bank?.....

2. How many branches does your bank have?

Less than 5 5-10 11-15 More than 15

3. What is your bank's ownership?

Local Government Foreign Other.....

4. Does your bank have an independent risk department?

Yes No Don't know

5. Does your bank make use of any risk software?

Yes

No

6. Which of the risks listed below does your risk department monitor (**Tick the ones which apply**)

Operational Risk

Credit Risk

Market Risk

Interest Rate Risk

Compliance/Regulatory Risk

Strategic Risk

Liquidity Risk

Foreign Exchange Risk

7. Does your bank have a strategic plan?

Yes

No

Don't know

8. If yes, what period in years does it cover?

1- 2 years

3-5 years

Over 5 years

9. Has your bank set aside specific budgetary allocations to fund risk management activities?

Yes No Don't know

10. Does your bank have a formally approved risk management policy?

Yes No Don't know

11. Who approves your risk management policy?

Board CEO Risk Committee Other

Section B: Strategic Risk Management.

12. Do you believe your current Strategic Risk Management practices support achievement of your bank's objectives?

Yes No Don't know

13. How important is an effective strategic risk management framework in achieving your bank's goals and objectives?

Very Important Marginally important Not important

14. Does your bank conduct risk identification during its strategic planning?

Yes No Don't know

15. Is your bank's strategic risk appetite and tolerance clearly documented?

Yes No Don't know

16. Does your bank have a board risk committee?

Yes

No

Don't know

17. If yes above, is the board risk committee combined with board audit committee?

Yes

No

Don't know

18. How often does the board risk committee meet to review the bank's risk profile and mitigation strategies?

Monthly

Quarterly

Semi-Annually

Annually

19. Who are the members of board risk committee? (Tick as many as are appropriate)

a) Non-executive directors

b) Independent directors

c) Chair of the board

d) Chief Risk officer

e) CEO

f) Other (Please specify).....

20. Who chairs the board risk committee?

Board chairman

Independent non-executive director

Other.....

21. Who is responsible for identifying the strategic risks faced by your bank? (Tick as many as are appropriate)

CEO

Board/ Executive Management

Risk Manager

Line Managers

All staff

Other.....

22. Does your bank have a strategic risk treatment plan?

Yes

No

Don't know

23. Are your bank's strategic objectives clearly communicated and understood across the bank?

Clearly communicated

Partially Communicated

Not Communicated

24. Has your bank developed its own strategic risk management reports which are used to monitor risks?

Yes

No

Don't know

25. Does your bank provide training to its management on strategic risk management?

Yes

No

Don't know

26. Has the bank integrated risk management philosophy into its culture?

Yes

No

Don't know

27. Does the bank's management clearly understand that the bank and its subsidiaries are exposed to strategic risk?

Yes

No

Don't know

28. Does management fully recognize the significance of self-assessment and ensure that the bank implements self-assessment adequately and reflects the results in various reports?

Yes

No

Don't know

29. Does your bank identify strategic risks in terms of

	Yes	No
a) What can happen?	<input type="checkbox"/>	<input type="checkbox"/>
b) How and why these risks arise.	<input type="checkbox"/>	<input type="checkbox"/>
c) Source of the risk	<input type="checkbox"/>	<input type="checkbox"/>
d) Level of impact if the risk crystallized	<input type="checkbox"/>	<input type="checkbox"/>

30. What criteria does your bank use to assess the impact of its risks?

a) Financial

b) Regulatory/Compliance

c) Reputation/brand

d) Others.....

31. Does your bank formally evaluate the effectiveness of existing risk management controls and the cost of controls?

Yes No Don't know

32. Does your bank have a strategic risk register?

Yes No Don't know

33. Are strategic risks in your bank analysed in terms of

	Yes	No
a) Likelihood	<input type="checkbox"/>	<input type="checkbox"/>
b) Consequence	<input type="checkbox"/>	<input type="checkbox"/>
c) Reputation impact	<input type="checkbox"/>	<input type="checkbox"/>
d) Financial impact	<input type="checkbox"/>	<input type="checkbox"/>
e) Level of impact if the risk crystallized	<input type="checkbox"/>	<input type="checkbox"/>

34. Which of the following method is used by your bank to measure and monitor risk?

a) Key risk indicators

b) Independent oversight by board on strategic risk related matters

c) Monitoring of the risk management program by internal audit

35. Kindly list down the types of strategic risks faced by your bank

.....

.....

.....

.....

.....

.....

.....

.....

36. Overall, at what stage of strategic risk management practice development do you consider your bank to be at?

a) Best practice

b) Well developed

c) Reasonably well developed

d) Basic

e) Non existent



37. Briefly highlight on the challenges you face in your strategic risk management practices.....

.....

.....

.....

.....

.....

.....

Thank you for your co-operation.