STRATEGIC RESPONSES USED BY EQUITY BANK TO COMPETE IN THE KENYAN BANKING INDUSTRY

BY

DEREK ARIEL ABISHUA

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Declaration

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

Signature...................................... Date...

DEREK ARIEL ABISHUA

(D/P/61/8503/2000)

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

Signature...................................... Date...

DR. JOHN YABS

Dedication

This project is dedicated to my mother Margaret Njeri Matigi to whom I owe so much. I highly cherish your love, encouragement, support, and guidance throughout all these years. Above all, thank you so much for training me to believe in myself.

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Abstract

The banking industry has experienced a rapid growth in terms of profits, deposits, revenues during the Kibaki's era. This trend has triggered a lot of competition in the banking industry. Equity Bank has managed to weather this competition to stand out as one of the most successful Kenyan businesses today. This paper analyzes the strategies that are being used by Equity Bank to compete in the Kenyan banking industry.

To achieve this objective, the study intended to use structured questionnaires; the target respondents were the senior employees of Equity Bank but the target respondents were not accessible. The researcher resorted to using secondary data for the study instead. The data was analyzed using both descriptive and inferential statistical analyses.

The study found that Equity Bank uses 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. The study found Equity Bank to be a very adaptive bank with a versatile reactionary mechanism to exploit any emerging gaps in the banking industry.

The bank has been able to create new markets in uncontested areas like hair salons, millet growing (for brewing) and dairy industry, so its competition strategies are heavily bent on using "blue ocean strategies". The study therefore concludes that Equity Bank has managed to build competitive advantages that can be exploited to sustain and further its growth.

Historically Equity Bank strategy was focused on the low end market segment however the bank has created now infrastructure and organizational structures and has included SME's and corporate banking in its evolving strategy.

The Equity Bank case study is relevant to people studying the following topics: Business in Kenya, bank pricing, marketing, micro-finance, bank business model, and strategy.

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List of Acronyms and Abbreviations

ATM	Automatic Teller Machine
CEO	Chief Executive Officer
CBK	Central Bank of Kenya
EABL	East African Breweries Limited
EBK	Equity Bank of Kenya
ESOP	Employee Share Ownership Programme
HF	Housing Finance
IT	Information Technology
ICT	Information and Communication Technology
IDB	Industrial Development Bank
IPO	Initial Public Offering
KES	Kenya Shillings
KNBS	Kenya National Bureau of Standards
KYC	Know Your Customer
MFI	Micro Finance Institution
NGO	Non Government Organization
NSE	Nairobi Stock Exchange
UNDP	United Nations Development Programme
SACCO	Saving and Credit Cooperatives
SME	Small and Medium Enterprises

CHAPTER I: INTRODUCTION

1.1 Background

In the aftermath of the Second World War, customers started to become more affluent and, as a consequence, more financially sophisticated. In response to these socioeconomic changes, banks, which had traditionally been supply-led, started to emerge as demand-led organizations (Howcroft 2005). The Kenyan banking industry experienced a similar phenomenon after the political and economic liberalization of the 1990's.

The managers today are facing an increasingly complex and dynamic environment (Chandan 1997). These dynamics have created hyper-competition in different industries. According to D'Aveni, 1994 hyper-competition is "characterized by intense and rapid competitive moves, in which competitors must move quickly to build [new] advantages and erode the advantages of their rivals". Factors that have led to accelerated hyper-competition include knowledge sharing (franchise and outsourcing), brand convergence, quick niche copying (imitation), and high quality resulting from standardization, shrinking markets, and attraction of powerful new entrants to business segments with high returns (Thomas and D'Aveni, 2004).

Competition continues to affect banks in Kenya and other countries. "From being the largest banks in the world in the inter-war period, the and big four' retail banks in Britain (Nat West, Midland-HSBC, Barclays and Lloyds-TSB) have seen their cosy-oligopoly gradually weaken since the 1960s. The banks have been rocked by the recession of the early 1990s and their exposure to bad debt while rounds of re-regulation and deregulation, such as the 1986 Building Societies Act, have blurred the boundaries between different financial specialisms and institutions"(Alexander and Pollard, 2000).

Competition in the Kenyan banking industry has risen, so much that even international banks like Barclays and Ecobank have been hawking their services. Banks haven't been competing blindly as profitable growth and efficiency have displaced the traditional emphasis on volumetric targeting and "size for size's sake" (Howcroft, 2005). Kenyan banks have had to develop strategies to respond to competition, to both safeguard their niches and to enlarge their market share.

Different firms have in the past used different competitive strategies to manage their businesses. Prahalad and Hamel (1990) notes that while in the 1980's the emphasizes was on restructuring and leaner organizations in the 1990's the focus was on identifying, cultivating, and exploiting core competences. The core competences model focused on the business as a portfolio a departure from the strategic business unit model championed by General Electric. They also note that business in the 1990's used the core competences model to exploit their competences and build strategic architect to secure their future.

Defining the industry in which competition actually takes place is important for good industry analysis, not to mention developing strategy and setting business unit boundaries (Porter 2008b). Equity bank's competition extends beyond the banking industry to cover competitors like cooperative movement, government financial institutions, merry go rounds, and micro finance institutions. Porter, 2008b also notes that a company strategist who understands that competition extends well beyond existing rivals will detect wider competitive threats and be better equipped to address them. However this research has been limited to the commercial banking industry and geographical scope limited to Kenya.

“Competition has always been contentious in banking. Regulators have traditionally tried to restrict competition in the sector with the aim of restricting excessive risk taking (Vives 2001)”. Not with standing their fears forces like globalization, liberalization, and technology have generated competition in the industry.

According to (Yildirim and Philippatos 2007) “a certain degree of competition is generally perceived to be essential and desirable to improve allocative and productive efficiency in the provision of financial services”. Yildirim and Philippatos, 2007 also notes that “a healthy rivalry among banks can serve as a driving force in improving the quality, pricing and availability of the products offered to customers, and promote financial innovation by introducing more modern banking skills, management techniques, and technology”.

1.1.1 Kenyan Banking Business Environment

Kenyan banks are operating in a more politically risky environment. The country's political rating was badly dented by the last general election. This has led to the downgrading of the country’s credit rating. “Fitch has given Kenya a long term ‘B+’ credit rating, a medium term ‘B’ credit rating and a ‘BB-’ local currency credit rating. Its revision of the country’s rating outlook came after another international rating agency; Standard and Poor’s (S&P), downgraded Kenya’s credit rating from ‘BB-’ to ‘B+’ (Gikunju 2008)”.

The Kenyan banking industry operates under a monopolistic competition market structure. It is dominated by Barclays, Citigroup, Kenya Commercial Bank, Standard Chartered, Cooperative Bank and lately Equity Bank with CFC Stanbic. Monopolistic structures may be beneficial to the economy as (Petersen and Rajan, 1995) demonstrates that young firms with no record of past performance may actually receive more credit, and at better rates, if they are in a market where banks have monopoly power. However, Thomas and D'aveni, 2004 have little regard for monopolistic competition as they believe its dead. They note that “monopolistic competition may still frequently occur at localized levels (for example, on certain city-pair routes in the airline industry or in certain therapeutic categories in the pharmaceutical industry), but only quite rarely at the industry level as a whole”.

One would expected this competition to have eroded the Kenyan banks supernormal profitability however the banks continue to register above average return on shareholders funds compared to their global counterparts and segments of the Kenyan economy. However this should not be viewed negatively as only financial sustainable institutions can guarantee the sustainable access for financial services to the micro, small business entrepreneurs including the farmers in both rural and urban area (Channy 2003).

The supernormal profits being underwritten by Kenyan banks have attracted foreign competition. Although Kenya is a relatively small economy, leading global banks like Citigroup, Barclay's, United Bank of Africa, Standard Bank of South Africa (trading as CFC Stanbic) and Standard Chartered have local subsidiaries. Foreign competition is useful as “foreign bank entry can stimulate competition in national banking markets and thus force domestic banks to improve their operating efficiency (Yilidirim and Phillipatos 2007)”.

An analysis of the current Kenyan environment reveals the economic challenges listed below which are affecting the banking industry. According to the Minister of planning the challenges for Year 2008 included post election disruptions, unfavorable, continued political bickering, weather conditions, high cost of food and fuel prices, high crude prices, and the global financial crisis (Kenya National Bureau of Statistics 2009). Any challenge can be converted to an opportunity, so its impact on individual banks will depend on the strategies used by its management to respond to the environment.

The rising inflation is likely to negatively impact on the Kenyan banking industry. The overall 12-month inflation increased from 21.9 percent in January 2009 to 25.1 percent in February 2009 due to increases in the prices of most of the seasonal food products. The 12-month underlying inflation was 8.7 percent in February 2009 (Central Bank of Kenya 2009a). This inflation is likely to erode the public purchasing power, something that can force customers to withdraw or consume their bank deposits.

The official usable foreign exchange reserves held by the Central Bank declined from US dollar 3,346 million (equivalent to 4.75 months of imports) as at March 05, 2008 to US dollar 2,626 million (equivalent to 3.13 months of imports) as at March 05, 2009 (Central Bank of Kenya 2009a). This foreign exchange decline is likely to lead to the depreciation of the Kenyan shilling. This will put pressure on banks to make higher profits, as they try to sustain positive growth in the eyes of foreign shareholders. Foreign shareholders evaluate performance from a hard currency perspective, so for a firm to sustain results reported previously they must make enough profits to cover up for the depreciation.

Kenya currency exchange rate has depreciated by 14.65% over the last 3 years to KES 80.20 as of March 15, 2009. This depreciation also means more monies will be needed to service the foreign debt. This is likely to force the government to borrow more funds or reschedule its debts. The Government gross domestic debt increased by KES 48.2 billion, from KES 430.6 billion in June 2008 to KES 478.8 billion as at February 27, 2009 (CBK 2009). The government is likely to sell more debt instruments which are likely to be attractive to banks than lending to the economy.

Prices of Equities' in the once vibrant Nairobi Stock Exchange have been on a downward trend. The factors that have led to NSE index deterioration include post election violence, declining profitability, and decimal performance Safaricom equity stock. The shareholders' wealth has been eroded from a high of KES 1.3 Trillion in June 2008 to 611 billion at the close of Feb. 2009 (Obonyo 2009). This is posing a serious challenge to banks trying to raise extra capital.

The Cooperative Bank was one of the first casualties with its listing IPO being under subscribed by 19%. The stock market decline is also likely to slow down the government effort to divest from state banks like Consolidated Bank, National bank, Housing Finance and Development Bank. The shrinking stock prices have also exposed Kenyan commercial banks, by eroding the value of their borrowing customer collaterals.

The massive layoffs in the economy have affected the banking industry forcing it to slow down its consumer lending. Some of the laid off borrowers are also likely to default their loan repayments. This will increase the size of the non performing loans in the industry. “A slow down in net loans advanced was apparent in the fourth quarter of 2008, out of a total KES 22.39 billion net loans advanced during the year, the fourth quarter accounted for only KES 1.3 billion reflecting tighter lending conditions across the banking industry (Kang'aru 2009).

In the third quarter the economy registered a reduced growth rate of 2.1 % compared to 6.3% in 2007. The forth quarter is expected to have had worse performance as the growth rate for the year is projected only at 2.8% (Kang'aru 2009). Wahome (2009a) puts the Year 2009 growth forecast at 3.5%. This slow down will certainly cascade to the banking industry. One of the tools being used to address the economic challenges by the government is the Vision 2030 strategy. It collaborates heavily with the manifestos of the main constituent parties of the grand coalition, however (Gakuru 2006) warns us that it isn't a government of the day project and we must insulate it from political competition.

The banking industry has responded to this changing business environment with several strategic responses. Most banks have reduced their lending especially to consumers. To substitute and supplement their lost revenues banks have started to invest heavily in government securities. While banks like Cooperative Bank, Ecobank, Family and Cooperative have adopted expansion strategy and are opening more branches. Other banks like Cooperative Bank, Diamond Trust and NIC Bank have resorted to regional expansion. Banks like Cooperative Bank, Family Bank, ABC Bank have broadened their product offering with an aim of transforming themselves to financial supermarkets.

The banking financial institutions in Kenya are predominately incorporated under the Companies Act Chapter 486 of Kenya Laws. However quasi-bank cooperative credit unions are incorporated under the Cooperative Act. The banks are regulated by the Banking Act, the Central Bank of Kenya(CBK) Act, Micro finance Act of 2006, and the supplementary operational guidelines issued by CBK. The banks and micro finance institutions also self regulates themselves through their lobby organizations bodies the Kenya Bankers Association and the Micro finance association respectively.

Banks in Kenya are competing for deposits, loans and advances. Competition is likely to intensify in the banking industry in the background of a shrinking economy. However, the industry low penetration level of 19% still provides opportunities for banks to exploit. Banks are also competing with mobile phone operators' money transfer services like Safaricom's (M-Pesa) and Zain's (Zap). M-Pesa service has over four million registered subscribers. It transferred over KES 24 billion its first year of operation (Njiraini and Anyanzwa 2009). Most banks have already introduced phone-banking services to counter this competition.

1.1.2 Banking Industry

Modern banking has been practiced in Kenya for the last 100 years. Kenya commercial bank recently celebrated its centennial celebrations last year. Since independence, the commercial banks in Kenya have grown both in number, branches, and the variety of services they offer like loans, credit and debit card services, and introduction of automatic teller machines (ATMs), electronic banking and other services (Lyaga 2006). In this period the banking industry, has experienced several upheavals that have lead to several reforms in the industry. This reforms are reflected in the 1994 Banking Act (and its amendments), Central Bank Act 1994, and other CBK regulations. These regulations are likely to reduce the impact of global credit crunch on Kenya.

As at March 31, 2009, the Kenyan banking sector comprised 43 commercial banks, 2 mortgage finance companies and 123 foreign exchange bureaus (Central Bank of Kenya, 2009b). Last year show the simultaneous mergers of CFC and Stanbic Bank, Prime Bank and Prime Capital and Credit. Kenya also witnessed the licensing of two new Islamic banks; Gulf African Bank and First Community Bank. Nigeria's United Bank of Africa also obtained a license to operate in Kenya.

The banks already listed at the Nairobi Stock Exchange include Standard Chartered, Barclay's, CFC Stanbic, Kenya Commercial bank, Equity Bank, NIC Bank, Diamond Trust, National Bank, Housing Finance and Cooperative Bank. Fidelity Bank, Southern

Credit Bank and Family Bank have also privately issued their shares to the public investors.

Kenya is considered to be over-banked as compared to other countries like Nigeria, which has less than 30 banks with a population of 130 million as compared to Kenya that has 45 banks and about 33 million people. However, Nigerian banks are much bigger than the Kenyan ones both in assets and branch network. The Finance bill of 2008 raised the requirement for banks' core capital from the current KES 250 Million to KES 1 billion by December 31st 2012. This is likely to force the low capitalized banks to merge lead to further consolidation in the industry. Other banks will be forced to collaborate with foreign banks like EABS with Ecobank of Nigeria. However, Equity Bank is not going to be affected by this directive as its capitalization stands above KES 26.5 billion. However, the likely consolidation will create larger banks and stronger competition.

According to CBK (2007) a survey conducted by the banking division of the Central Bank of Kenya in 2007 revealed the following aspects ranging from product usage to challenges in gaining access to financial services. Only 19 percent of Kenyans are banked and thus have formal access to financial services through commercial banks, building societies and Post Bank, and an additional 8 percent are served by SACCOs and MFIs and 35 percent depend primarily on informal financial services such as ROSCAs (Rotating Savings and Credit Associations) and ASCAs (Accumulating Savings and Credit Associations). The study also revealed that access to financial services varies across the country and is highest in Nairobi, which has the greatest number of bank branches (194 out of 443).

Kenyan incorporated banks have embarked on regional expansion to the East African community and beyond. So far, at least six local banks – Equity, Kenya Commercial Bank, Fina and Diamond Trust Bank are operating in regional markets with prospects of further expansion within the year (Wahome 2009b). Other banks with regional presence not include in his list are Barclays, Standard Chartered, Stanbic, NIC Bank, and Equatorial Bank. Cooperative Bank has also announced that it planned initial entry into Southern Sudan and Uganda before the close of the year. This expansion will create several Pan-African banking chains that will offer strong competition to Equity Bank.

Kenyan banks have been diversifying their product offering to other areas like bank assurance, mortgages and investment banking. This form of diversification is not unique to Kenya as it has been practiced in other countries like United Kingdom (Howcroft 2005) and USA (Cetorelli 2001). After the passage of the Financial Services Modernization (Gramm**.**Leach**.**Bliley) Act in 1999, that allowed the operation of commercial banking, investment banking, and insurance underwriting within the same holding company. This is likely to be affected by the changes in the financial markets that will be put in place by Obama administration to deter the repeat of the credit crunch.

Commercial Banks in Kenya have also made very heavy investment in information technology. Modern banks are very dependent on technology. Banks use technology to operate their communication networks, operate ATMS, and offer e-banking services among others. These systems are operated by very expensive ERS (Enterprise Resource Systems) like Oracle, SAP and Flexi-cube, which cost several million dollars. Kenya Commercial Bank spent US$ 6 Million in 2002 on its controversial system upgrade (Karkhanis 2002).

There is significant change in customer's landscape due to the unprecedented interest in individuals, micro finance sector and SME's (small and medium scale enterprises). The banking industry had previously had a bias for corporate clients. Equity Bank is a market leader in this segment but must have a strategy to sustain this position.

1.1.3 Equity Bank

Equity Bank was started in 1984, as a building society in Murang'a, with a focus the mortgage sector. Its expansion necessitated the conversion to a bank in December 2004. Equity Bank is one of the biggest indigenous local banks, a status it has managed to achieve in just a space of 25 years. It initial target market was Muranga's tea zone. The tea zones were an easy target, as they had no powerful cooperatives offering banking services. The bank has been focusing on small-scale farmers, individual customers and small and medium scale businesses. The bank has now moved to other segments like corporate banking, mortgages, and investment banking.

The bank has continued to consolidate its position in Kenya, as at the end of February the bank had 3 million customers and 106 branches. Chiou, 2009 provides empirical evidence that building a branch network enables a firm to favourable compete due to increased proximity and resulting convenience. Equity branch expansion has been duplicated by other banks like Barclays, Cooperative Bank, Ecobank, Bank of Africa and Family Bank.

The bank has also aggressively expanded to the Great Lakes region, where it intends to replicate its Kenyan model. Equity bank also aims at further grow its market share by raising its stake at Housing Finance and acquiring the government's 23% stake in National Bank. If successful, Kenya's banking industry will be lead by two indigenous banks, Equity Bank and Kenya Commercial Bank.

“The board is the soul of a company. Sound corporate governance has a lot to do with a board’s structure, decision-making style, and efficiency (Barton, Wang, and Ye 2009).” While Minichilli, Zattoni, and Zona (2009) notes the six main tasks of an effective board as service (advice, networking and strategic participation) and control (behavioural, output and strategic control). With respect to advice and counsel, the board of directors should actively evaluate and select strategic alternatives developed by top managers and supply suggestions to improve the quality of strategic decision making. Equity Banks' highly experienced board is well positioned to perform all the above tasks.

The Bank has 7 Board committees that guide and govern its management. These committees are Audit, Credit, Risk management, Strategy and investment, Tendering and procurement, Governance, board nomination and staff remuneration, and board executive. The Chief Executive oversees the day-to-day running of the bank and is assisted by several whole time executive directors.

Equity Bank mission is to “Mobilize savings, term deposits and other funds for the efficient provision of loan facilities to the micro finance and missing middle sector, especially small and medium enterprises, to generate sufficient and sustainable profits, in order to contribute to the members’ welfare and to the national economy”. From its mission its strategic focus in terms of the scope of product, market, geographical area and which strategy it intends to use to achieve competitive leadership.

This strategy is geared towards making banking services accessible to a vast majority of Kenyans who presently do not use or have access to banking services'. The Bank has focused on providing comprehensive financial services and solutions to the low and medium income segments of the population. This market niche is composed of micro entrepreneurs, salaried and wage workers, small-scale commercial farmers, small and medium enterprises, and all eligible private individuals.

The Directors believe that the bank will continue to experience growth over the next few years and plans to adopt a growth consolidation strategy with objective of ensuring that the Bank remains financially sound, strong, and competitive in the provision of products and services. The bank intends to reinforce its institutional structure by ensuring that financial resources, information technology, human capital, infrastructure and other core resources are a level needed to respond both to internal and external challenges. Coupled with the growth consolidation strategy, the bank proposes to diversify and offer new but complementary services within its current market and expand into the East African and other regional markets in Africa where the Bank is able to replicate its model. This diversification will be achieved through both acquisitions of existing businesses and organic growth (Equity Bank, 2007).

Equity Bank has grown strategically by successfully making the following acquisitions purchase of the retail business arm of Industrial Development Bank (IDB) in 2005, 20% of Housing Finance in July 2007, and 100% acquisition of Uganda Micro Finance Ltd. In June 2008 Equity Bank increased its stake in Housing Finance to 24.9% through a rights issue.

Equity bank has advanced plans to expand to Southern Sudan. Equity Bank and Kenya Commercial Bank have used a “first mover” strategy to expand into Southern Sudan. Tu and Sullivan, 2009 uses the case Carrefour in China to pin point the challenges of this strategy. They recommended that for a firm to succeed it should exploit its external and internal environmental factors that are usually firm-specific.

However "first mover" strategy has its own benefit considering people always remember the first timers like Columbus, Armstrong, and Speke. Eisenmann, 2006 notes that for "first mover" strategy to be beneficial the firm must be able to create entry barriers and enjoy "winner take all" benefits. He warns that if such barriers are lacking intense rivalry will follow leading to erosion of supernormal profits if any.

Equity bank has expanded its initial products like personal savings and loan accounts offered by the building society to include trade finance, treasury services, personal banking, corporate e-banking, cash back services, short message services banking, retail Internet banking, swift codes, business loans, mobile banking, automatic teller machines, insurance, investment banking, and custodial services. Loan products include overdrafts, hire purchase, premium financing, asset financing, bills discounting and financing, trade finance and collateral management, cheques discounting, and "fanikisha" loans for women.

Despite the growing competition in the financial services sector the bank has continued to record impressive performance on several parameters. The banks five-year financial summary shows that the bank profits before tax grew from KES 218 M in 2004 to KES 5,022 M in 2008 or 2304%. The banking sector's profit before tax increased by 34.6 percent from KES 20.4 billion in July 2007 to KES 27.4 billion in July 2008 while Equity bank's grew by KES 2.643 Billion(111.10%).

This growth was the highest among the listed banks in 2008. Equity Bank Group total assets grew from KES 6.7 Billion to KES 78.8 Billion. The growth from 2007 to 2008 was KES 25.7 Billion (48.39%), this better than the industry that expanded by KES 288.9 billion (33.8%) from KES 853.7 billion as at July 2007 to KES 1,142.6 billion as at July

2008 (CBK 2008a). It also has the lowest nonperforming loans to total loans ratio in the industry.

Equity Bank can be classified as an international business by the fact that it has invested in other countries like Sudan and Uganda, its is involved in foreign exchange and trade credit services and has several international shareholders like British America Insurance (BAICL), Helios Capital and AfriCap. AfriCap is a consortium of international investors led by International Finance Corporation and European Investment Bank. This active participation of foreign investors is believed to be an expression of the highest level of optimism on the bank's future both in the short and long term as well as a confirmation of the bank's position as an attractive investment.

1.2 Statement of the Problem

There is a gap between theoretical background and operation of the strategic responses used by Equity Bank in the face of competition in the banking industry. “Large diversified firms have been a dominant factor in the economies of many developing countries. Nonetheless, they have received only limited research attention, so the knowledge in this area is limited (Nachum 1999)”. The only study carried on Equity Bank so far is Munga (2005), which focused on managing resistance to change in the banking industry in Kenya.

Similar studies include Ohaga (2004): A study of the strategic responses of Commercial banks in Kenya to changes in their environment and Karambu (2004): The strategic responses to changes in the environment by the Co-operative Bank of Kenya Limited. This research is different to Ohaga (2004) by scope and with Karambu (2004) by focus.

If strategy research is to continue to offer credible guide-lines on the strategic behavior of firms it seems imperative to have a more fundamental under-standing of the factors influencing a firm's choice of diversification strategy and how this evolves in response to changing business conditions (Weirsema and Bowen 2008). The problem therefore is to find out the strategic responses used by Equity Bank to compete in the Kenyan banking industry.

1.3 Objectives of the Study

The objective of this study is to determine which strategies are being used by Equity Bank to respond to competition in the Kenyan banking industry.

1.4 Significance of the Study

This study will be important to the various users of this research information who will include government regulators, Equity Bank, other banks, investors and academia.

This study will be very valuable to the regulators like Central Bank of Kenya considering the pivotal position played by Equity Bank in the Kenyan banking industry; according to CBK (2008b) Kenya had 4.5 million bank customers as at September 2008 and by the end of February 2009 Equity bank accounts had over 3 million accounts. This implies that Equity bank currently controls over 50% of all the bank accounts in Kenya. Other regulators who may be interested in Equity Bank case study include Kenya Bankers Association and Capital Markets Authority.

This study will also be useful to investment bankers and investors (existing and potential) as it will give them gainful insight on the Equity Bank business model. The value of extra business information can be appreciated by the recent collapse of very celebrated businesses like AIG and Lehman Brothers. "For decades, AIG was the world's biggest insurer, a company known around the world for providing protection for individuals, companies and others. But in September, the company would have gone under if it were not for government assistance (Gethard, 2009)."

This research will be beneficial to Equity Bank in that it will expose the gaps in its strategy, which if addressed in time will help it to deter competition. It will also identify the strategies it can leverage to sustain its competitive edge. The study will also make significant contribution to current and potential investors of Kenyan banking industry, as it will provide a lot of insight on the strategies they can use to respond to competition.

This research will add to the existing body of knowledge in this area and stimulate further research on different aspects of response to competition in various industries.

CHAPTER II: LITERATURE REVIEW

2.1 Strategy

The use of the term strategy in business dates only to the twentieth century, and its use in a self-consciously competitive context is even more recent (Ghemawat, 2002). Strategic management as a discipline originated in the 1950s and 60s (Wikipedia, the free encyclopedia). The concept of strategy can be traced to military where it applied in war. The business world adopted this concept in the nineteenth century (Angulu 2007).

Military strategies adapted by businesses' include the US navy's networking critical path. Among other things strategy aims at establishing a competitive domain for the firm by defining its business and what it intends to be. Strategy also guides a firm on issues like growth, diversification, investment and divestment.

Strategy defines the expected contribution of the various functions in the realization of the firm's strategy (Hax and Majluf 1991). Due to its importance, strategy is the work of the chief executive and may take as much as 80% of his time. In implementing and communicating the strategy the chief executive is assisted by the department heads who oversee their respective functional strategies. For strategy to succeed the Chief executive must ensure all the functions have goal congruence. This ensures all managers pull together without any of them hindering or contradicting the effort of the others.

The strategies being used by Equity Bank to respond competition in the banking industry include diversification, talent, ICT, marketing, and financial strategies. Diversification has been widely studied in economics, management, and finance. The literature on bank structure suggests both efficiency and agency rationales for diversification (Klein and

Saidenberg, 1998). Diversification strategies have involved the broadening of product offering range and the geographic diversification strategy pursued by Equity Bank, which has enabled the bank to expand to two neighboring countries apart from internal expansion in Kenya. It is evident from the literature reviewed that Equity Bank has been able to increase its market share both locally and regionally through acquisitions.

Equity Bank marketing strategies have focused on retention of existing customers as well as recruitment or mobilization of new ones. It is evident from the study that Equity Bank has been able to increase its market share both locally and regionally. As at May 2009, the bank has over 106 branches and over 3 million customers.

All this success by Equity Bank would not have been possible without funds to finance growth and expansion. For firms operating in a highly competitive environment a distinctive strategic orientation is needed, requiring the exploitation of critical resources in order to gain competitive advantage (Bernard & Koerte 2007). One way Equity has been able to support this effort is by building reserves of over KES 26.5 Billion.

2.1.1 Industry Analysis

Awareness of the five forces helps a company understand the structure of its industry and stakeout a position that is more profitable and less vulnerable to attack (Porter 1979, 2008). In his article he notes that the five forces model helps one to look beyond his direct competitors. Porter, 2008 notes four competitive forces that can hurt profits: savvy customers that can play you and your rivals, powerful suppliers who may constrain your profits by charging high prices, aspiring entrants armed with new capacity and hungry for market share, and substitute offerings that can lure your customers away.

For the firm to benefit from the five forces model it must be able to comprehensively define its industry. Porter, 2000 states that "defining the industry in which competition takes place is important for good industry analysis, not to mention for developing strategy and setting unit boundaries". To this end he notes that the firm must determine the product and geographical scope and identify the players and segment under the four segments listed above. The analysis should also assess the strength and weaknesses of these competitive forces. It is also crucial to understand the industry profitability and the recent positive and negative developments in the industry.

Porter, 2008 concludes that "the five competitive forces reveal whether an industry is truly attractive, and they help investors anticipate positive and negative shifts in the industry structure before they are obvious". He also notes that this deeper thinking about competition is a more effective or superior method to achieve investment success than financial projections and trend extrapolation that dominates today's investment analysis.

The five forces model will make Equity Bank sensitive and reactive to what is happening in the banking and beyond. This will help the bank to adapt to changes and developments in sectors like mobile banking, cooperatives, insurance and investment banking. Strategy doesn't just focus on expansion, once moribund companies like Nokia and Disney have had to use divestment strategies to reinvent themselves to today's success stories. Through this strategy they divested their loss making operations and focused on the profitable ones. Strategy may also help to broaden the firm's market size. Gillette for example, which had 60% of razor blade market by redefining its market to men's grooming products, was able to uncover new opportunities for growth.

2.1.2 SWOT Analysis

Beyond understanding the industry, a detailed analysis of a firm's strengths, weaknesses, opportunities, and weaknesses is necessary to understanding the improvements needed to improve its competitiveness. “An internal analysis of strengths and weaknesses will identify the unique skills and resources that give an organization a competitive advantage. Unique competitive advantage is a combination of superior efficiency, superior quality, superior innovation, and superior customer responsiveness (Chandan 1997)”.

Its Strengths include a wide branch network of over 106 branches as at March 10, 2009, vibrant information technology network built to support over 35 million customers, strong balance sheet with a capital base of over KES 27 Billion , one stop shop – financial supermarket offering(insurance, investment banking, mortgages, and traditional banking, over 3 million loyal customer base, a strong board of directors pooling experienced professionals from diverse sectors, strong innovation business culture and strong reliable supply of low cost funds.

One major weakness with Equity bank is the issue of high dependency on its Chief Executive. James Mwangi seems to be the soul of Equity Bank. Any dent on his reputation would negatively hurt the banks' stocks and at worst cause a depositors runoff. The Equity Bank brand is synonymous with the Kikuyu tribe and low end clients something that puts off other tribesmen and the high net worth clients. Its other weaknesses include lack of experienced staff and a high labour turnover.

While the opportunities available for Equity Bank include reduced foreign competition as foreign banks are slowed by global recession, expansion into investment banking services, corporate banking services, asset finance services, credit card business, and phone based money transfer services. The bank can also acquire the National Bank, which is being privatized. Regionally it can expand to Rwanda, Burundi, Congo DRC, and Tanzania.

Threats facing Equity Bank include economic slow down and entry of the heavily capitalized Nigerian banks into the market. The researcher will in this paper explore the efforts that have been made by Equity Bank to exploit the strengths and opportunities and to reduce the threats and weaknesses. Other threats that the bank needs to overcome include credit risk, operational risk, inflation risk and liquidity risk.

2.2 Competitive Strategy Frameworks

There are no established universal methods for tackling competition. Different times and industries use have successfully used different methods or strategies. Among the models advanced by scholars to tackle competition include competitive advantage, delta model, customer intimacy and blue ocean strategy.

2.2.1 Generic Strategies

One of the foremost authors to use term comparative advantage in his literature was David Ricardo in 1817 in his book "The Principles of Political Economy and Taxation". His application was built on specialization focused on the economy and not the firm. Thomas and D'aveni, 2004 quotes several researchers who all agree that comparative advantage enables a firm to out perform its competitors in profitability or performance. These returns are similar to Ricardian rents.

According to Hoffman, 2000 the earliest reference of comparative advantage to firms can be traced Alderson's article in 1937 on "A Marketing View of Competition." in the Journal of Marketing. According to Alderson the fundamental aspect of competitive adaptation is the specialization of suppliers to meet variations in buyer demand.

A firm builds competitive advantage when it creates or develops attribute/s or resources that enable it to outperform its competitors. Porter, one the leading authorities on competition recommends that a firm should use one or a combination of generic strategies to compete.

By leveraging on the generic strategies the firm is able to earn above average return (supernormal profits) on its assets. This supernormal profit gives the firm competitive advantage over the other firms in the industry. Supernormal profits ensure the firm can withstand onslaughts in the industry like price wars.

Competitive advantage is, in very basic words, a position a firm occupies against its competitors (Wikipedia, the free encyclopedia 5/18/2009). Sources of competitive advantages include government subsidy or support, monopolistic markets, innovation, operational efficiencies, superior service offering and highly skilled human capital.

Porter, 1994 notes that the three generic strategies used to compete at business unit level are cost leadership, differentiation and focus. Cost leadership enables a when a firm delivers the same services as its competitors but at a lower cost e.g. Wal-Mart. Differentiation advantage enables a firm to delivers superior product same price or lower price than its competitors e.g. Toyota's Lexus brand. Equity Bank has tried to brand and differentiate its products like Autobank (ATMs) and Cash back (debit card).

Under the focus strategy a firm concentrates its marketing effort on a narrow market segment (market niche), aiming at achieving a local rather than industry wide competitive advantage e.g. Porsche has concentrated on luxurious sports cars. Equity Bank mission statement emphasizes the bank bias to focus on the unbanked, micro-finance, and small and medium enterprises. However this strategy seems to have been modified as the bank has redefined its markets to include insurance, investment banking and also established a corporate department in its structure to address the high end market.

Competitive advantage is not a perpetual state; firms must work to sustain their advantages as the competition will play catch up. Competitive advantage is built upon set of conditions that are invalidated or reinforced as dynamics change in the environment. These advantages are not universal and change with times. The strategies Ford used to compete with General Motors (GM) were very different with the ones used by Toyota to dislodge GM its market leadership.

2.2.2 Customer Intimacy Strategies

Treacy & Wiersema, 1992 uses customer intimacy to explain the competitive strategies used by firms like Nike, Dell Computer, and Home Depot to successfully rise and grow to world class brands. They note that these businesses succeeded by redefining customers' value in their respective markets, building systems that delivered more value than competition and also by raising customer's expectation way beyond the reach of competition. According to them, these firms achieved leadership in their industries by narrowing their focus.

They focused on delivering superior value by operational excellence, or customer intimacy, or product leadership. By operational excellence firms aims at delivering products or services at competitive prices and with minimal difficulty or inconvenience. Customer intimacy involves providing products to match the firms segment and target markets. Product leadership involves offering leading edge products that render rival goods obsolete.

They also note that through operational excellence a firm like Dell has been able to under-cut Compaq and other PC makers without compromise quality. They also cite the direct connect program was successfully used to transform and reinvent the General Electric (GE). Customer intimacy firms continually tailor and shape products and services to fit an increase definition of fine definition of the customer. Companies that pursue product leadership strive to produce a continuous stream of innovative products like Apple's Ipod and I-phone or Sony's Walkman.

2.2.3 The Delta Model

Another competitive strategy model that approaches strategy from the customer perspective is Prof. Anorldo Hax's delta model. According Hax 2009, “Well, conventionally, all of the major frameworks of strategy start by recognizing the essence of strategy to achieve superior competitive advantage. That is what everybody adheres to. We found that that as a concept and as a mindset is extremely dangerous, and it is because it puts competitors at the center, and if you do that, then there is a tendency to watch over your shoulder or in front of you, who is running behind or ahead of you, and you try to imitate them.”

Hax, 2009 asks” if the competitors are not at the center then, who is at the center? For us, the answer was obvious. The customer is. Therefore, the customer is the driving force. You have to start deeply understanding what the customer requirements are and how you can help the customer in the most effective way, and then it changes completely the ways in which you are figuring out what actions to do. Now, instead of trying to imitate somebody, you are trying to separate yourself from the rest of the pack. You try to produce a value proposition, which is unique, which is differentiated, which adds value to the customer and expresses a great deal of customer care, customer concerns, and that value proposition should be based on mutual trust, mutual learning, mutual benefits, transparency. Can you imagine the difference in mindset? Instead of strategy as war, the Delta Model tells you strategy as love".

According to Hax & Wilde II, 2003 the three distinct strategic positions of "The Triangle," or delta, the model are best product, total customer solutions and system lock-in. Under the best product positioning, the primary focus is to attract, satisfy, and retain the customer through the inherent characteristics of the product itself. Total customer solutions aim at providing solutions that consist of a portfolio of customized products and services that represent a unique value proposition to individualized customers. System lock-in aims at creating a dependency on your products by the market. An example of a firm that enjoys system lock-in is Microsoft, where customers want to buy the computer with access to the largest set of applications, and software developers want to write applications for the computers with the largest installed base.

According to (http://www.dean.com/about_us/delta_framework.htm) the System Lock-in strategic option has the widest scope; it includes the extended enterprise — the firm, the customers, the suppliers, and most importantly, the key "complementors". A complementor is a firm that engages in the delivery of products and services that enhances our own product and service portfolio. The key to this strategic option is to identify, attract, and nurture the complementors. The complementors are often external, but may also be internal to the corporation, particularly in large and diversified organizations. These complementors are rarely detected and exploited effectively. That is why a system lock-in strategy has to start with a full corporate scope — not just for one product or business — and has to continue with the identification and incorporation of all the key external players that can become complementors.

2.2.4 Blue Ocean Strategy

Blue Ocean Strategy is a way to make the competition irrelevant by creating a leap in value for both the company and its customers. Kim and Mauborgne 2004 challenges everything previously considered as the basis for good strategic success, and instead argues that the way to win is to stop competing. Their success stories include the [yellow tail] brand of Australian winery Casella Wines which took only two years to skyrocket to position number 1, in the fiercely competitive U.S. market for imported wine.

According to them most companies are making mistakes by battling for success in the bloody "red ocean" where rivals fighting over a shrinking profit pool. In the red ocean, industry boundaries are defined and accepted, prices are driven lower, and the competitive rules of the game become known. As the market space gets increasingly crowded, prospects for profits and growth decline. In the red oceans, industry boundaries are defined and accepted, and the competitive rules of the game are known.

To create blue oceans, Kim and Mauborgne 2004 argue that companies need to use an opposite approach. Instead of benchmarking with the competition, they should set their own rules and create "blue oceans" of uncontested market space ripe for growth. In blue oceans, demand is created rather than fought over. There is ample opportunity for growth that is both profitable and rapid. In blue oceans, competition is irrelevant because the rules of the game are waiting to be set. Blue Ocean is an analogy to describe the wider, deeper potential of market space that is not yet explored.

By changing their strategic thinking and using a systematic approach, the authors' show how companies can reach beyond existing demand to find a blue ocean of new market space with the potential for huge profits and growth. This strategy offers an inspiring message: that success is not dependent on fierce competition, expensive marketing or R&D budgets, but on smart strategic moves that can be used systematically by established companies and startups alike. The tools they describe level the playing field for success. At a time when global competition is intensifying and supply exceeds demand, this landmark work will chart a bold new path to winning the future.

There are numerous initiatives that would suggest that Equity Bank has borrowed from the blue ocean strategy model. One example is its joint venture with EABL to finance sorghum growing in Ukambani. Another example of blue ocean strategy is its opening of branches in "unbanked" parts of the country like Kariobangi, Githurai, Kayole and Rongai.

2.3 Competitive Responses

The strategies being used by Equity Bank to respond to the competition in the Kenyan banking industry include diversification and improvement its value chain. According to Mintzberg, 1994 strategy making is not an isolated process limited to strategy planning meeting. To the contrary it is interwoven with all it takes to manage an organization.

2.3.1 Diversification Strategies

Diversification refers to expanding business fields either to new markets, new products, or both, while retaining strong core businesses (Yokoyama 2007). Diversification has not been limited to the banking industry, retail chains have also successfully diversified to banking. In Kenya mobile phone companies have also diversified into money transfer services.

Frequent and successful new products introductions are essential for organic growth and competitive differentiation. The numbers of new product introductions have increased dramatically across the globe (Davis 2007). Equity Bank has not also been left behind in this race. It has managed to introduce new innovative services like “Autobank” automatic teller machines and “Cashback services” that have made it more competitive by increasing the revenues generated from its existing customers.

“Cashback services” enables customers to use Equity bank ATM cards to pay for services or access cash from outlets like supermarket chains. “Cashback services” model, is an innovation that borrows heavily from Visa and MasterCard card networks.

Equity Bank has also diversified its products offering by introducing comprehensive banking services, forex products, insurance, investment banking, and mortgage services. Not all businesses have had to diversify their offering to grow or compete. Successful global corporations like Wal-Mart and McDonald's have profitability grown just focusing on one line of business. Advocates of this strategy believe if you get it right first time you don't have to change. Another example is FedEx, that hasn't moved in tandem with its industry rivals like DHL, UPS and TNT other areas of logistics like clearing and forwarding but has stuck to small parcels (Roberts, Roberts and Ward 2005).

Diversification may focus on related or unrelated areas. Equity Bank has also adopted unrelated diversification strategy by extending its offering to beyond commercial banking to other areas like banc-assurance, mortgages, and investment banking. Banc-assurance refers to distribution of insurance products and services through a bank. The insurance business is handled by Equity Insurance Agency Ltd that was formed in May 2007. The agency already has 93 employees and underwrote a premium of KES 500 Million in 2008 which is very significant considering the total insurance industry premiums in 2006 amounted to Kshs. 41 Billion (Akumu 2009).

Banc-assurance is expected to get entrenched route in Kenya as the following other companies are associated by common ownership AIG Insurance and Commercial Bank of Africa, Kenya Orient Insurance and Family Bank, General Accident and Investments and Mortgages Bank, ICEA and NIC Bank, and Mercantile Insurance and Ecobank. The entry into insurance is in line with Mr. Mwangi's (Chief Executive) vision of turning Equity into a one-stop financial services supermarket (Akumu 2009).

The diversification has also extended to other areas like investment banking through acquisition of custodial services license. Due to reluctance by Capital Markets Authority to issue new investment banking licenses Equity bank acquired Juanico Investment Bank in January 2009, the deal enabled the formation of Equity Investment Bank, an outfit that will offer structured financing and financial advisory services as well as unit trust products (Makau 2009). However, Equity Bank has declared that it won't venture directly into stock broking. This is unlike its competitors like NIC bank, Chase Bank, ABC Bank, and Cooperative Bank who own the following brokerage houses NIC Capital, Ghengis Capital, ABC Capital, and Kingdom Securities respectively.

Equity bank has also formed alliances with several businesses across the globe to enable it expand its product offering. Equity Bank is one of the banks distributing the Western Union money transfer services in Kenya. The bank has also established an alliance with global correspondent banks to enable its customer's to transact business globally.

Equity bank has also formed an alliance with UAP insurance to distribute its health insurance; they have branded the product “Equihealth”. This diversification strategy in response to competition has help Equity Bank to develop a bunker strategy “sheltering” its customers from competition by creating a financial supermarket. Through such offering the bank has also become more competitive by increasing their profitability yield per customer.

Equity Bank strategic alliance includes various correspondent banks, stockbrokers and international visa card network. Such alliances enables the bank have a wide outreach network at a competitive price. The bank is also a major player in the Western Union cash transfer network. Locally the bank has created alliances with firms like Kenya Power and Safaricom.

2.3.2 Business Acquisition Strategies

Business acquisition strategy is one of the strategies used by companies to beat competition by accelerating their pace of growth. Firms can strategically benefit from mergers and acquisitions by acquiring new customers and markets, cost reductions through synergies and obtain new products or technologies (SAP 2008).

Mergers and acquisitions are the most popular form of growth strategy according to a survey by Boston Chapter of the association for corporate growth conducted in New

England USA. Other proponents of this strategy are Welch & Welch (2005) and Gaughan (1999). Growth aspects include market penetration, market development, product penetration and diversification (Ansoff 1965).

Equity Bank has responded to competition by rapidly growing its business through a series of acquisitions. Acquisitions include the purchase of the retail business arm of Industrial Development Bank (IDB) in 2005, 20% of Housing Finance from CDC group in July 2007, 100% acquisition of Uganda Micro Finance Ltd for KES 1.66 Billion in April 2008.

In June 2008 Equity Bank increased its stake in Housing Finance to 24.9% through a rights issue. Kenyan economy has only 22,000 mortgages compared to its population of 40 Million people. Equity Bank wants to replicate its experience in retail banking in the mortgage sector.

These series of acquisitions have helped build a very strong network with enormous capability to respond to the competition in the Kenyan banking industry. The resulting transformation has helped Equity Bank move from the position of a reactionary bank to a mover and shaker in the banking industry it is today.

2.3.3 Value Chain Strategies

The term ‘Value Chain’ was used by Michael Porter in his book "Competitive Advantage: Creating and Sustaining superior Performance" (1985). The value chain analysis describes the activities the organization performs and links them to the organizations competitive position. Porter argues that the ability to perform particular activities and to manage the linkages between these activities is a source of competitive advantage. Porter distinguishes between primary activities and support activities.

Primary activities are directly concerned with the creation or delivery of a product or service. They can be grouped into five main areas: inbound logistics, operations, outbound logistics, marketing and sales, and service. Each of these primary activities is linked to support activities which help to improve their effectiveness or efficiency. There are four main areas of support activities: procurement, technology development (including R&D), human resource management, and infrastructure (systems for planning, finance, quality, information management etc).

2.3.3.1 Financing Strategies

Equity Bank has responded to financial strength of its competition by inviting extra shareholders/investors at its various growth stages. In the initial periods the bank had relied on its founding shareholders, their friends and people from Kangema but it later opened up to outsiders, by the time its listing in 2006, Africap a foreign fund already owned 4%. This strategy has given it funds that have helped it to grow faster than the more closely owned competitor's like Family Bank.

In November 2007 Equity bank offered 24.99% stake to EBS Helios through a private equity deal that raised KES 11 billion. In the same year it also secured international loans amounting to KES 8 billion from China. These two injections and its then existing shareholders funds of KES 3 billion raised its core capital to KES 22 billion as at November 15, 2007.

This formed the largest private direct foreign investment in Kenya so far and turned Equity Bank into one of the most capitalized bank in the local banking scene, higher than Barclay's Bank which had a capital base was standing at KES12.3 billion (Omondi

2007). With a KES 22 billion capital base the bank's maximum lending capacity was raised up to KES 5 billion up from the previous ceiling of just KES 750 million".

Equity Bank was able to strategically execute the "Helios Deal" to raise extra capital without having to go through the "pains" of an IPO. This was a well thought strategy than competition considering that the recent Cooperative Bank IPO was under subscribed by 21% even though its was raising half of what Equity Bank got from the Helios Deal.

The move should also be lauded as it protected their shareholders wealth. Helios Capital being a long-term investor had no effect on Equity Bank free float shares. The limited supply of free float helped the bank to continue enjoying among the highest P/E (price earning) ratio at the NSE. The shares of Cooperative bank have been on a downward trend due to excess free float despite its more favorable P/E ratio.

Profit maximization is one of the objectives of operations of commercial firms and hence they have to decide what level of output generates optimum returns. To maximize profit firms use the optimizing output technique specifically by minimizing average cost of production (Dwivedi 2002)". One way banks make themselves competitive or more profitable is by ensuring that they have a cheap source of long-term funds to fund their business. This is usually achieved through mobilization of cheap deposits.

To this end, Equity Bank has been reaching to the wealthy pockets of the nation like the tea belt and other rural areas. In such areas depositors' main incentive of keeping monies in the bank, is mainly safety. So they are easily satisfied with low returns. Such cheap funds have enabled the bank to lend at better margins than its competition.

Equity bank hasn't been paying all the earnings to shareholders as dividends but has been retaining some of these profits. As at the close of 2008 the bank had accumulated retained earnings amounting to Kshs19.54 Billion. Such reserves provide a cheap source of funds for the bank. Its undistributed reserves are among the biggest in the banking industry today.

Equity bank has also borrowed overseas where interest rates are lower than Kenya, however this strategy can be risky due to exchange fluctuations. Depreciation of the local currency can wipe all the savings from such borrowings. Banks cushion themselves from such exposure by hedging e.g. Development Bank has hedged with KCB their KES 3 billion development loan from China.

Equity Bank have been authorized by its board to exploit such opportunities and borrow long term loans of up to KES 4.52 Billion from various international development financial institutions (Equity 2007). Banks in Kenya have also been accessing cheap funds by offering to administer state funds for youth and women development. Equity Bank has already borrowed KES 100 million from the Youth Fund for further disbursements to the youth.

The Bank has also tapped cheap funds by developing channels to handle development funds from donors, which usually attracts very low interest rates. Through such an initiative in 2007, Equity Bank collaborated with UNDP to launch a women development product known as "fanikisha" (Equity 2007). Other international bodies working with Equity Bank include International Fund for Agriculture-IFAD and Alliance for Green Revolution in Africa – AGRA.

2.3.3.2 Marketing Strategies

Equity Bank has adopted several marketing strategies to respond to the competition in the banking industry. Equity Bank has embarked on several tactics to build an effective marketing strategy to tackle its competition in the banking industry. These tactics include customer acquisition, distribution, pricing, advertising, branding, relationship management, innovation customer satisfaction, and social marketing strategies.

Equity bank has responded to competition in the banking industry by creating a strategy to acquire more customers from the unbanked population and from rivals to increase its market share. In the 1990's Kenya' economy was performing very poorly due to then prevailing global recession. This situation forced several international banks to restructure their local operations. ABN Amro Bank opted to move out and sold its local operation while Standard Chartered and Barclays had massive layoffs and branch closures.

Equity Bank exploited this scenario by moving in to possess the “abandoned customers” in the affected towns like Murang'a and Limuru. Equity Bank has also outsmarted competition by building its customers by focusing on the unbanked masses by opening branches in the unexploited or untapped areas. Such areas include the wealthy tea zones of Central Kenya Highlands and “previously disregarded” suburbs like Kayole, Kariobangi, Rongai and Githurai. Through this strategy Equity Bank managed to enlarge its market without having to confront competition from the big banks.

During this recessionary period of the 1990s many Kenyan banks positioned themselves as corporate banks and had little time for individuals, and small and medium scale enterprises segments. Equity bank exploited the situation to grow its customer base by focusing on this “abandoned market segment”. As the bank had very little competition in this segment this enabled it to generate supernormal profits from this niche for almost a decade until the other banks returned attracted by its rosy performance. The profits generated from this period boosted the bank competitive capabilities.

Equity bank has also strategically grown its customer base by simplifying the process of opening and making itself the most convenient bank to bank with. While other banks were demanding a minimum amount to open a bank account Equity Bank allowed customers to open accounts with nil balances. While other banks were demanding "unreasonable documentation" from their customers in pretext of KYC (know your customer) rules Equity Bank used a more friendly approach. It appreciated that some of its customer's were lay people that were currently living as tenants who had no utility bills and resorted to other references from farmers' societies and employers.

Such sensitivity to customers has also generated goodwill for the bank through word of mouth advertising. However in the post Helios deal the game plan seems to be changing. The bank now has a fully-fledged corporate banking department so it is very likely to adopt a very different strategy in its next development phase. This aggressive drive for customers has also increased the bank market share.

The researcher is of the opinion that Equity uses a radically different model compared to competition to evaluate its distribution channels. Christopher (1994) defines the channel of distribution as the means whereby products are physically transferred through the system and through which acquisition takes place. While other banks require each branch to be a viable cost center(strategic business units) in terms of lending and liabilities, Equity Bank seems to be looking at the larger picture so it doesn't seem to mind collecting deposits in one area and deploying them elsewhere and not prejudice either branch when evaluate their viability.

From this it seems that that Equity Bank is tackling the competition by playing the game with a different set of rules with its competitors. This approach would make it harder for competition to predict it. Asian companies successfully used a similar strategy in the past to successfully their competition in the West. Many changes are taking place in the supply and distribution environment, which have a radical effect upon the market position of a business (Kiumbura 2003).

"The prices of the competition may influence the price strategies of any bank. The clients will evaluate the price by comparing the products of many organizations. Any price strategies in banking marketing company must know the price and quality of the competition products and use the information in establishing their own prices when there are offered similar services, of close quality and value, the price must be comparable to the one practiced by the closest competition, otherwise the organization risks the loss of sales (Cetina and Mihail 2006)".

However it is interesting to note that this theoretical notion is being challenged in the Kenyan banking industry as Equity Bank the most profitable bank yet is also the most expensive bank (CBK 2008c). Equity bank has benefited greatly by avoiding price wars by protecting its profitability. "Price competition transfers profits directly from an industry to its customers. Price cuts are easy for competitors to see and match, making successive rounds of retaliation likely (Porter 2008)". Equity have also managed to charge premium prices by playing in markets "deserted" by other banks in terms of geographical locations and business segments.

Competition in the banking industry has also led to sudden interest in advertising by previously rather silent banks like Bank of Africa, Diamond Trust and Fidelity Bank. Equity Bank has also aggressively pursued its promotion campaigns, becoming one of the most covered businesses by the Kenyan media today. Its media coverage has taken both paid and non-paid advertisement. Although the researcher has no evidence to show any causal link between new accounts opening with its advertising, he believes it has played a significant role in the rapid growth of new account holders.

Advertisement has also played a crucial role in strengthening the Equity Bank brand. “Branding is important to both customers and the marketer. To consumers point of view branding facilitates buying. They are also guaranteed quality when they are buying brands. Consumers also get psychological satisfaction when buying brands, especially when products give them desired status. To a marketer, a brand differentiates firm’s products from those of competition (Kiumbura 2003)”.

Some banks have decided to compete by developing new products or by differentiating their existing products from competition or new innovations. For example kids saving account has been differentiated as follows junior mover (NIC Bank), Mdosi junior (Family Bank), Just for me (Diamond Trust), and Jambo junior (Cooperative Bank). Cash dispensing automated teller machines have also been differentiated as follows Autobank (Equity), Cashpoint (Cooperative) and ATM Standard Chartered Bank.

Equity Bank re-branded Microfinance Uganda after acquisition and will expand to Southern Sudan in its brand. However it has allowed Housing Finance to retain its identity. Chinese companies like Huawei and Lenovo have successfully exported their brands, but firms to invest in building the brand. Lenovo's high-profile marketing efforts have included major sport sponsorships — the Beijing Olympics, the US National Basketball Association, and Formula One racing for instance — as well as prominent exposure to global mass-market business magazines (Dietz, Orr, and Xing 2008).

Interest rate movements, saturation in some credit businesses, active capital markets, and increasing customer awareness of emerging technologies are forcing banks to look for alternative and innovative product lines and service delivery channels. Innovation is the process of developing new products to meet customer needs more efficiently. "An innovation is a product that is new to the market or simply new to the adopter. An invention is a discovery or process of doing new things or transforming creative ideas into useful applications. It is important to remember that of the total resources required for innovation only a small proportion comes from invention the majority comes from design, production, marketing, and the rest of activities that contribute to the making of things (Wambui 2006)".

Even with the existing diversification among the Kenyan banks traces of dominance in certain segments can still be felt in the industry. Market segment consists of a large identifiable group within a market with similar wants, purchasing power, geographical location, buying attitudes, or buying habits (Kotler 2001). The target market refers to particular groups of customers to whom the company wishes to appeal. To the identified target group the firm develops a market offering, e.g. Volvo has positioned itself to satisfy safety while Jaguar and Rolls and Royce have aimed at satisfying the luxury status.

A company can produce products for different segments. This market segment is the unique piece of the total market that the business can claim and defend because of competitive advantages (Pearce and Robinson: 2002). Equity Bank still continues to dominate the individual and small-scale businesses segments. The bank is slowly tackling other markets have started to segment its customer's by opening categorized branches like corporate branches for medium businesses and prestige branches for the very big firms. Some firms operate in sub segments known as niche markets e.g. Porsche. Niche markets are a typically small market whose needs are not well served with the rest.

Equity Bank has adapted social marketing strategies to respond to the competition in the banking industry especially the “Anti-Kikuyu” undertones by emphasis on goals that extend benefits beyond the bank to the society, which encourages further support from government bodies and the public. Such strategies would also explain its investment in agricultural fund and its many rural branches. The bank has also developed close links with politicians from all divides. The bank has endeared itself so much to the system that its Chief Executive is the Chairman of the delivery/implementation arm of the highly regarded National Social Economic Council, a position here he reports directly to the President. The bank has also aggressively recruited employees from other communities. It is also running an alumni program that absorbs all the best KCSE students from the country districts as interns. The bank has also incorporated in its board of directors people from all major tribes.

The bank has responded to competition by developing “armies” of relationship managers in their organizational structures to boost customer retention and satisfaction. Although this strategy has been widely replicated in the banking industry, Standard Chartered and Citigroup are clear leaders. This strategy has favored these two banks due to the focus on corporate segment, which has few customers but very high revenues per capita so they can afford such attention profitably.

Relationship management ensure that the bank keeps across watch on its customer's and reacts to any threats by competition on time. Equity bank has also started to hire relationship managers. The researcher expects the bank to accelerate this concept as its corporate division picks in the market.

2.3.3.3 Information and Communication Technology Strategies

Jayawardhena & Foley, 2000 noted that deregulation and technological developments were the most important external drivers of increased competition and change in the financial services market. A part from relying on the physical distribution network Equity Bank has exploited ICT and e-commerce to create a virtual distribution network. This has been a strategic response to the competition in the industry, as all the banks in Kenya are today involved in E-commerce one way or the other. Bajaj and Nag (1999) notes that "Electronic Commerce (E-Commerce) has unleashed yet another revolution, which is changing the way businesses buy and sell products and services. It is associated with buying and selling of information, products, and services over computer communication networks."

By 2000, over 40,000 Kenyans had ISP accounts and an estimated number of computers at 250,000 with about 600 websites and a total of 50 Internet service providers licensed to operate in the country and Kenya has its share of Internet users with an estimated figure of 300,000 users (Wanjoga 2001). "An ICT strategy gives technological direction and purpose, organizes and deploys IT (information technology) resources in the most effective manner, and coordinates the stream of decisions being made by different members of the organization and IT function. Strategy is about aligning every activity to create an offering that cannot be easily emulated by competitors (Kitur 2006)".

He also notes that “it is also apparent that developments in ICT are transforming most aspects of the organization including organizational structure and design, the value chain and nature of products/services offered and the markets served among others. ICT is also redefining the relations between the companies and its customers and suppliers and changing the whole industry structure.

For employees to be effective, they need to be supported by an excellent and adequate information system. Most firms have moved from just basic information systems to enterprises resource systems (ERS) that have integrated most of their operations. Some ERS join even the suppliers and customers in the value chain. This helps in making sure that all the decisions are based on informed decisions, as information is readily available. Leading enterprise resource systems include oracle, SAP, Microsoft Dynamics, and PeopleSoft have been embraced by all the leading firms, with Oracle running almost all the Forbes 500. Equity bank has realized the importance of ICT and invested in one of the biggest ICT infrastructure in Kenya by acquiring an ERS (Enterprise Resource System) that can handle up to 35 million customers.

The bank has utilized this ICT to have competitive advantage over other banks in serving the local market and the Kenyan Diaspora. ICT has also enabled the bank to develop innovative products with competitive advantage like cash-back services and efficiently handle its bulk custodial services business. ICT also provides a platform for the bank to compete on cost competencies. To boost innovation in ICT and E-Commerce Equity Bank can learn and benchmark with global leaders like Amazon.com.

A systematic cross-country analysis of E-commerce activity reveals that although physical infrastructure ex-plains much of the variation in basic Internet use, e-commerce activity also depends significantly on a supportive institutional environment. Chief among the characteristics of such an environment are national respect for the "rule of law" and, secondarily, the availability of credible payment channels such as credit cards (Oxley and Yeung 2001). These results suggest that an institutional environment that facilitates the building of transactional integrity is critical to the development of e-commerce.

The Kenyan government has actively addressed the legal challenges by enacting the Communication Act. It has also licenced two other fiber-optic submarine cable companies to connect Kenya to several Internet hubs and end dependency on the much slower satellite link. Kenya has a well-established credible payment system dominated by Visa card that is operated by all the big banks including Equity Bank. Other credible payment channels include mobile phone companies' money transfer systems, Postal Corporation System and Equity Bank's “Cashback” network.

2.3.3.4 Customer Care and Operation Strategies

Equity Bank business model is built around customer focus. Its business tag line is “A listening, caring, business partner. The bank has endeavored to create a culture to reinforce this strategy. Equity Bank has adapted an open-door marketing strategy where its Chief Executive and Marketing Managers are very easily accessible to its customers.

Equity Bank has also created a fulfilling working environment by developing an organizational architect that empowers its staff even at branch level. This strategy not only generates job satisfaction but also generates customer satisfaction due to the swift decision-making. Firms have now realized that long-term growth and survival is dependent on a good relationship with customers.

Banks in Europe and elsewhere agree that branch network will remain the cornerstone of their retail distribution strategy (Bidmead, Massoud & Romanoswki 2007). Equity bank appears to have adopted this strategy as it has built one of the most extensive branch networks in Kenya. Banks endeavor to use such branches to reach and satisfy its customers. Although building such a branch network is very expensive and some of the expansions or refurbishments have no clear payback (Bidmead, Massoud & Romanoswki, 2007). So they suggest that banks should lay emphasis on managing customer visits.

Among the methods recommended by Bidmead, Massoud & Romanoswki 2007 to manage customer visits includes customer surveys, online banking and utilization of automated teller machines. Equity Bank has adopted online banking and installed a huge network of ATM branches. However Equity Bank has adopted a loner model and has been reluctant to join other ATM networks like KDN data network and Pesa point. Equity bank has also been a front runner in the mobile banking. Its mobile banking system is branded "Benki mkononi 247".

Real strategic change requires reinventing new categories, not arranging old ones (Mintzberg 1994). Innovation is one of the best ways to respond and shake giants, as it enables small firms to achieve what was always thought to need many resources. An example is the article by Otis Port on Business week (Feb 2, 2004) pp.54, showed that how NASA one of the best-funded organization in the planet is being challenged through innovation by smaller firms like Space Exploration Technologies Corp and Scaled Composites LLC in making better and cheaper crafts to fly to the Moon/Mars.

Equity Bank innovations include the launching of an in-house point of sale system (cash back) instead of adopting the visa electron debit cards by banks like National Bank and

Cooperative bank. Its other innovations include the exploitation of custodial services to levels never previous seen or imagined in the Kenyan financial sector. Through other risk taking innovations like drawing against “uncleared cheques” the bank has been able to create a lucrative stream of income and endeared to its customer who considers such services a great favor.

Although Equity Bank innovation culture is remarkable it still have along way to go considering that 3M one of the Worlds most innovative companies of all times , according to the editorial of Businessweek (April 7, 2004) pp. 64 has been for years been generating over a third of its annual profits from new products. 3M's success had been in taking commercial advantage of unexpected scientific discoveries like floppy discs, sand paper, and post-it pads.

Damanpour, Walker & Avellaneda (2009) notes four types of innovation namely service innovations, process innovations, technological process innovations, and administrative process innovations. All the types of innovation should be continuously incorporated in the Equity Bank innovation strategy to ensure that it remains responsive and competitive. For innovation to yield optimum impact, firms must invest in market research to understand the industry, competition and customer’s expectation. Close interaction with customers provides one of the most effective platforms for such market research.

“You must deal with today's customer and tomorrow's customers. They provide the ideas for new products and new applications. They provide the early warning signals about your products' quality and timeliness. They know about your competitors. To know your customers is to know your future (Fox, 2000)”.

According to Drury, 2000, measures for innovation which include, Percentage of sales from new products; New product introduction versus competitors; New products introduction versus plan; Time to develop next generation products; Number of key items in which a company is first or second to the market; and Break-even time, being the time from product development work until the product has been introduced and has been able to pay back the investment.

2.3.3.5 Human Resource Strategies

Ammo (2003) emphasizes that “human resource is the most important factor for success in any organization. Lee and Miller, 1999, also notes that one of the key resources needed to execute an organization strategy is its human capital. Therefore, a dedicated and talented workforce may serve as a valuable, scarce, non-imitable resource that can help firms execute an appropriate positioning strategy. In their study of Korean businesses how an organization’s commitment to its employees’ well-being (OCE) can aid in the profitable execution of its positioning strategies.

Lee and Miller (1999) found that OCE, by itself, sometimes has a weakly positive association with return on assets (ROA). But far more important, we found that ROA is strongly and positively influenced by the interaction between OCE and the dedicated pursuit of Porter’s (1980) strategies for achieving competitive advantage: these are cost leadership, marketing differentiation and innovative differentiation.

“Yet the astonishing reality is that most of the firms are as unprepared for the challenge of finding, motivating, and retaining capable workers as they were a decade ago. Business leaders are deeply concerned, judging by two McKinsey Quarterly global surveys. The first, in 2006, indicated that the respondents regarded finding talented people as likely to be the single most important managerial preoccupation for the rest of this decade. The second, conducted in November 2007, revealed that nearly half of the respondents expect intensifying competition for talent - and the increasingly global nature of that competition - to have a major effect on their companies over the next five years (Guthridge, Komm & Lawson 2008)".

Equity Bank SWOT analysis reveals that, one of its weaknesses as lack of an "experienced" workforce compared to its competition being a relatively young bank. The management of Equity Bank has addressed these gaps by "poaching" from other banks and making heavy investment in training. However, according to the year 2007 financial report this relatively young bank has strategically accumulated wealth of experience through strategic recruitment of staff and directors.

The bank has managed to attract experienced staff from other banks and reputable world-class companies. Among the notable recruits from competition include Samuel Karugu-Marketing and Product Director (15 years with Glaxo Smithkilne), Peter Makau, Corporate Director (20 years experience at senior level with major local and international banks including Citibank N.A., ABN Amro Bank N.V., Standard Chartered), and John Njoroge-Finance Director from Standard Chartered.

The bank has also addressed its talent gap by enrolling in capacity building programs. They have trained their staff in leadership and management development programs offered by leading world business schools like Harvard Business School, IESE Business School in Spain, Strathmore Business School and Boulder Microfinance Leadership Program (Equity 2007).

Another challenge that has been facing the banking industry in the area of human capital is high labor turnover. Labour turnover takes critical dimension because it affects on the success of human resource plans. This is why it is important to pay attention to labour turnover in the sector in view of developing plans to attract, motivate and retrain the workforce (Andisi 2006). The rapid growth of Equity Bank has given it an edge over competition by providing higher job satisfaction than other bank through opportunities for career growth and this is now making it a sought after employer.

Equity Bank also distinguished itself from competition, as a choice employer by becoming one of the first listed companies in Kenya to have an ESOP scheme. Other ESOP schemes in Kenya include Access, KCB, Safaricom and East African Breweries. ESOP refers to an employee shares earning scheme. Such shares are offered at a discount but can only be accessed after a number of years of service. The ESOP has helped motivate and retain its staff. Through such efforts Equity Bank has built a competitive advantage over its competition through a deliberate strategy of creating a young energetic, well trained, and motivated work force.

Equity Bank will also need to reinforce its HR capabilities to handle the challenges arising from mergers and acquisitions. “People issues may be important, but they are historically the most difficult to resolve. Staff cannot be forced to cooperate, to drive forward merger objectives, or to change their business behaviour. They must be motivated and given incentives to do so. This requires careful planning, and resorting. Many companies have neither the resources nor the know-how to give this area the priority it requires (Kelly, Cook, and Spitzer 1999)”.

CHAPTER III: RESEARCH METHODOLOGY

3.1 Research Design

This section set out the research methodology used in this study to meet its objectives of identifying the strategic responses being used by Equity Bank to respond to competition. A case study design was used.

3.2 Data Collection

The study used mainly the secondary data to collect data from published sources such as newspapers, websites, annual financial statements and the financial performance data available at the Nairobi Stock Exchange. The secondary data was supplemented with primary data collected through a structured questionnaire administered on a drop and pick basis. The questions used, was hybrid of similar surveys by Munga (2005) and Njoroge (2006). Another primary data source was observation by the researcher during visits to various Equity Bank outlets. This was also supplemented with the Chief Executive's recent interviews with the media.

3.3 Data Analysis

The questionnaire data was checked for accuracy and completeness of recording of the responses, it was coded and checked for coding errors and omissions. The data was analyzed to bring out specific issues about strategic responses to competition. Quantitative analysis techniques such frequencies and cross tabulations were used to analyze the data. The findings were categorized using the four themes in the questionnaire.

CHAPTER IV: DATA ANALYSIS AND FINDINGS

4.1 Number of Respondents

The questionnaire was sent to Equity Bank's Chief Executive who forwarded it to the Human Resource Director, to coordinate the response from the heads of departments. However, there was no response to the questionnaires (Appendix). This forced the researcher to turn to solely to secondary data and various media coverage’s especially interviews with the Chief Executive by various media houses both in print and audio/visual and from the company’s published profiles.

4.2 General Information

This section generally covered the general information on the bank in the study. The specific information covered includes ownership, number of employees and staff diversity.

4.2.1 Ownership

This section was aimed at determining the bank ownership structure. The researcher found that that the bank was had 9,560 shareholders as at the close of December 31, 2008. The shares were distributed as follows.

Table 1: Ownership Structure

Equity Bank Ltd			
Ownership Structure			
As at December 31, 2008			
Rank	Shareholder Name	Shares	%
1	Helios EB Investors	90,516,255	24.45%
2	British-American Investments	41,910,289	11.32%
3	Nelson Muguku Njoroge	22,545,255	6.09%
4	James Njuguna Mwangi	19,898,505	5.37%
5	John Kagema Mwangi	15,139,690	4.09%
6	Equity Bank Employee Shares Ownership Plan (ESOP)	15,018,400	4.06%
7	Andrew Mwangi Kimani	10,928,040	2.95%
8	Fortress Highlands Limited	10,101,000	2.73%
9	AIB Nominee A/C Solidus Holdings	9,011,400	2.43%
10	Peter Kahara Munga	6,469,379	1.75%
11	Other 9,550 shareholders	128,739,489	34.77%
Total		370,277,702	100%
Source 2008 Equity Bank Financial Statements			

4.2.2 Size of the Payroll

This section was aimed at establishing the size of the firm payroll. The researcher found that the bank had 1,818 employees as at June 30, 2009. Its payroll had risen from Kshs 289 Million in 2004 to Kshs 2,954 Millions in 2008 according to the information extracted from its financial statements.

Table 2: Payroll Costs 2004 to 2008

Equity Bank Limited					
Payroll Costs					
Year	2004	2005	2006	2007	2008
Staff Costs	289	532	959	1,469	2,954

Source: Audited Accounts 2004-2008

4.2.3 Diversity of the board of directors

This section was aimed at determining how many nationalities and ethnic communities are included in the bank board?

- The researcher found that the bank had 13 Directors with the following composition of ethnic groupings.

Table 3: Ethnic grouping composition of the Board of Directors

Composition of the Board by Ethnic Grouping		
Ethnic Grouping	Number	%
Kikuyu	6	46.15%
Luyia	2	15.38%
Luo	1	7.69%
Kalenjin	1	7.69%
British	2	15.38%
Senegalese	1	7.69%
Total	13	100.00%
Source 2008 Equity Bank Financial Statements		

The researcher also found that the bank board of directors the following composition of nationality composition.

Table 4: Composition of the Board of Directors by Nationality

Composition of the Board by Nationality		
Nationality	Number	%
Kenyan	10	76.92%
British	2	15.38%
Senegalese	1	7.69%
Total	13	100.00%
Source 2008 Equity Bank Financial Statements		

4.3 Business Acquisition Strategies

This section was aimed at determining the businesses acquired by Equity Bank to enable compete in the Kenyan banking industry.

- The researcher found that the bank acquisition so far include:-

1. IDB Corporate banking business division between March 18 and April 22, 2005 for over Kshs. 57.3 Million (Equity Bank Kenya 2006).
2. During the year 2008, the Bank acquired 4.9% more shares at **Housing Finance** through a rights issue resulting in a total shareholding of 24.9% (Equity Bank Kenya 2008b).

3. 100% acquisition of Uganda Microfinance Ltd at a value of Kshs. 1,666 Million (Equity Bank Kenya 2008a).
4. Juanico Investment Bank

- The researcher found that the bank rationale for acquisition was:-

1. Housing Finance was aimed at replicate its retail banking success in financing low and medium income housing. In one of the TV interviews the Chief Executive said that the bank believes that Kenya housing industry is a big business as the country has a deficit of over one million houses. According to the Managing Director of Housing Finance Mr. Frank Ireri the deal offered the investing parties a good channel to sell their long term funds (Kwama 2007).
2. Uganda Microfinance was its preferred choice in Uganda due to the similarity in their market targets. According to Equity CEO Dr. James Mwangi, "the monumental deal fitted hand-in-glove with the Bank's growth strategy and that the choice of the acquisition and market was critical in the long term strategy. Since the investment by Helios EB, they had been actively engaged in strategically consolidating their dominant banking position in the country and seeking prudent regional entry points" (Equity Bank Kenya 2008a).
3. The bank bought Juanico Investment Bank as it needed a licence to capitalize in the Kenyan capital market and the Capital Markets Authority (CMA) was reluctant to issue new licenses (Makau 2009).

4.4 Growth and Expansion Strategies

This section focused on the growth and expansion strategies applied by Equity Bank to compete in the Kenyan Banking industry. To analyze this researcher reviewed the branch structure, proposed expansion and the benefits accruing from the growth and expansion

- This section was aimed at determining the bank branch structure. The findings are presented in tables below.

Table 5: Branch Network

Kenyan Banking Industry				
Impact of branch and ATMs network on profitability				
A review of the 4 Big Kenyan Banks				
Bank	Branches	ATMs	Kshs Millions PBT (Jun-09)	Kshs Millions Profit per Branch
Equity Bank	145	585	2,700	19
Kenya Commercial Bank	182	220	3,641	20
Barclays Bank	117	238	4,516	39
Cooperative Bank	63	212	1,940	31
Average	127	314	3,199	27

Source: Un-audited results Half Year 2009 published in the Daily Nation

- The researcher found from the bank website that the branch network covers Kenya, Uganda and South Sudan.
- According to the banks website it is supplementing its branch network with alternative channels like:-
    - Visa branded ATM's in Kenya
    - Points of Sale (POS) where customers shop; pay and withdraw cash in leading retail outlets.
    - Internet and mobile banking channels

- The researcher also through a visit to some of the Nairobi branches observed that the bank had also established strategic alliances listed below to enable them compete:-

1. Equity bank has partnered Western Union to offer money transfer services especially to the Kenyan Diaspora.
2. Equity bank offers Visa debit and credit cards to its customers.
3. Equity bank and UAP insurance have jointly been offering various health insurance products.
4. Equity bank uses various Stock brokers and investment banks to buy and sell securities for its custodial accounts in the Nairobi Stock Exchange.
5. British American Insurance Kenya Limited (Britak) joint venture in Housing Finance. Britak is also the preferred underwriter for the business underwritten by Equity Insurance Brokers.
6. Equity Bank has also partnered with various supermarkets (Tuskys, Uchumi, and Nakumatt) to offer “cashback” services to its customers.

4.5 Value Chain strategies

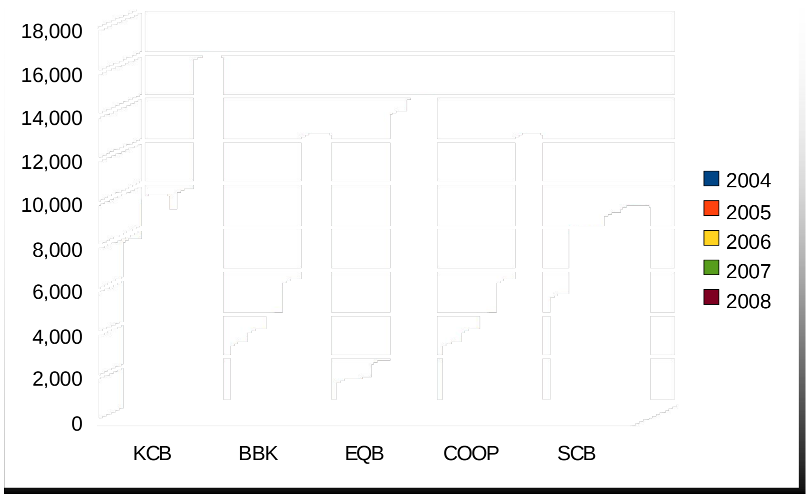
This section generally covered the general information on the bank in the study. The specific information covered includes ownership, number of employees and staff diversity.

4.5.1 Financing Strategies

This section was aimed at determining the financial strategies the bank is using to compete. The researcher analyzed the bank's balance sheet, dividend policy, and management of new investment partner.

Table 6: Growth in Core Capital (5 Years Trend)

Growth in Core Capital (Kshs Millions)					
Bank	2004	2005	2006	2007	2008
KCB	7,810	9,802	9,169	10,046	16,187
BBK	2,973	3,605	4,361	5,882	12,613
EQB	1,283	1,413	2,201	13,666	14,272
COOP	2,973	3,605	4,361	5,882	12,613
SCB	5,191	8,388	8,367	8,967	9,332



Source: Banking Survey 2009

- The researcher found that financing strategies like "Helios deal" has enabled the bank grow its core capital faster than industry as demonstrated by the table below.

Table 7: Core Capital Growth Comparison of Various Banks

Bank	2004	2008	Increase	% Growth
KCB	7,810	16,187	8,377	107%
BBK	2,973	12,613	9,640	324%
EQB	1,283	14,272	12,989	1012%
COOP	2,973	12,613	9,640	324%
SCB	5,191	9,332	4,141	80%

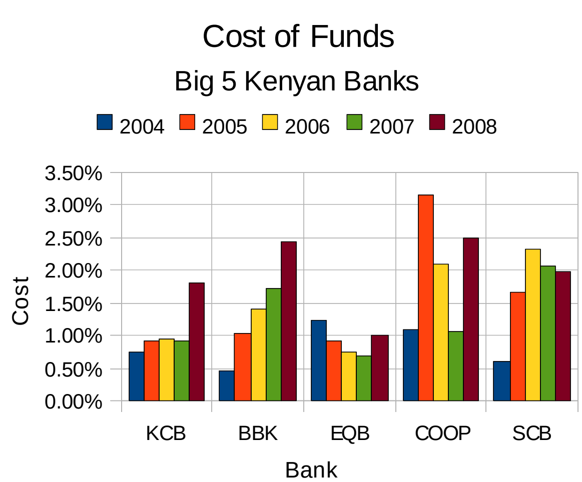
Source: Banking Survey 2009

- The researcher found that Equity Bank have managed to obtain funds at a lower costs than its competitors as demonstrated in the tables below.

Table 8: Comparison of the Cost of funds incurred by different local banks

Cost of Funds (%)						
Bank	2004	2005	2006	2007	2008	Average
KCB	0.75%	0.92%	0.96%	0.92%	1.80%	1.07%
BBK	0.45%	1.03%	1.41%	1.71%	2.43%	1.41%
EQB	1.25%	0.91%	0.74%	0.68%	1.01%	0.92%
COOP	1.10%	3.15%	2.09%	1.07%	2.51%	1.98%
SCB	0.60%	1.67%	2.33%	2.07%	1.97%	1.73%

Source: Banking Survey 2009



Source: Banking Survey 2009

- The researcher found that one of the sources of these cheap funds was profit retention. "Equity has had a consistent dividend policy of up to 40% of par-value. The Bank's Board of Directors intends to maintain a consistent annual dividend policy to the shareholders of an amount that can be sustained taking into account the variations in earnings and which is commensurate with the capital expenditure of the Bank (Equity Bank Kenya 2006)". Its dividend payout ratio has been less than 30% based on the information tabulated below since listing in 2006. This is very conservative as KCB has had a payout ratio of 43% since 2003.

Table 9: Equity Bank Dividend Payouts for 4 Years

Equity Bank Limited				
Dividend Payout Ratio				
Year	**2005**	**2006**	**2007**	**2008**
Profit after Tax	346	753	1,890	3,753
Dividend Paid	181	181	543	1,111
Percentage Paid	52.3%	24.0%	28.7%	29.6%

SOURCE : Financial Statements 2005 to 2008

- Has the positioning of your bank as a micro-finance institution helped attract low priced funds or capital from organizations like Africap? Yes ____ No____ (Tick as appropriate)?Yes
    - On 22nd April 2003 Equity Building Society the predecessor of Equity Bank Limited allotted 2,000,000 ordinary shares of Kshs. 5.00 each to Africap Microfinance Fund Limited ("AfriCap" or "AfriCap Fund") at a price of Kshs. 60.00 per share (Equity Bank Kenya 2006).
    - According to 2008 financial statements the bank had borrowed loans amounting to Kshs 6,463 Million at an effective interest rate ranging from 1 %

to 14.18%. Its biggest lender is FMO which is a Dutch owned organization that supports microfinance based development (Equity Bank Kenya 2008b).

- How do you manage to attract key shareholders like Helios and Africa without losing control?
  - Equity Bank board managed to limit the powers of Helios by signing an agreement (Memorandum of Understanding) that put a cap on their shareholding at 25% and limiting their seats in the board to their proportional ownership (Equity Bank Kenya 2007).

4.5.2 Marketing Strategies

This section was aimed at determining what the bank's marketing strategies were. To determine this researcher analyzed the bank's marketing department structure, target market, correspondent network, product mix, and product development.

- The researcher found from the company website that the bank had a fully fledged marketing department headed by the director of marketing, advocacy and public research. The bank structure also has other directors playing a crucial role in marketing like the directors of corporate banking, Product Development, Innovation and Research, retail banking, and the General Manager of alternative business channels. Marketing department is staffed by relationships and business development managers (Equity Bank Kenya 2008b).
- Marketing strategies being used by Equity bank are aimed at creating new marketing niches instead of confronting the existing market. "Through research and product innovation, Equity has developed products and services that identify the needs cycle and financial resources of this market segment thus carving out a

niche market. The Bank's target market which includes individuals, micro, small and medium enterprises is largely un-banked. The Bank's planned expansion targets this unexploited market. It is expected that providing financial services to this target market will result in continued growth in terms of business volumes and profitability (Equity Bank Kenya 2006)."

- Among the innovative products introduced by Equity Bank include:-

1. In November 2006 Equity Bank launched a facility of Kshs 500 Million offer credit to New KCC milk farmers against delivered milk. "This deal between Equity Bank and New Kenya Cooperative Creameries (KCC) means that farmers will be able to borrow between KShs1,000 and Kshs 500,000 for farm development, animal feeds, veterinary services and increase of their stock. (Wahome 2006)".

2. "Through its social approach to banking, Equity bank has rolled out unique products and services to support farmers in commercializing farming through affordable financial products. Equity has been partnering with various development partners in the private and public sector to support the agricultural value chain (Equity Bank Kenya 2009a)". One such initiative is a joint venture to modernize and commercialize small scale farming in Kenya, where local small scale farmers will access credit facilities from Equity Bank to finance modern agricultural inputs from Amiran Kenya. These Global GAP compliant agricultural inputs, which meet the highest standards of the European Union, include drip irrigation, farmer's green houses, quality seeds, fertilizers, agrochemicals, and tailored training from Amiran's team of expert agronomists, all packaged into the Amiran Farmer's Kit (Equity Bank Kenya 2009a).

3. Launch of a product, dubbed "**Laptop Ni Lazima**" by the bank in partnership with Safaricom to make acquisition of laptops and broadband modems more affordable. Under this partnership Equity Bank will provide credit to Safaricom customers to buy laptops with broadband modems (Equity Bank Kenya 2009c).

4. The researcher observed that Equity Bank has major events social events like the annual drama festivals, Olympic Games, and internship employment for the two best students in every district. The bank has also launched a fund for the recovery of the endangered Mau forest by donating Kshs 5 Million (Equity Bank Kenya 2009b).

5. The bank has also invested a lot of money in rebranding in its member campaign which has been being aired in the prime time by several media houses. The "Am a member advertising campaign" aims at identifying the bank with different gender, professions, age groups, regions and ethnic groups. The researcher has also observed that the bank has also put up a countrywide bill boards display to advertise and spread this campaign.

4.5.3 Information and Communication Strategies

This section was aimed at determining the strength of the bank's ICT. The researcher noted that, "In 2005, Equity invested over Kshs. 565 million on Information Technology infrastructure with Infosys, the world's leading core banking solution, which will support the Bank's expansion strategy. The Information Technology infrastructure includes a new generation core banking system, state of the art data centre and an enhanced Automated Teller Machines network (Equity Bank Kenya 2006)".

- Strategies being used to reach the Kenyan Diaspora include:-
  - Customer recruitment drives in the UK and USA.

- Provision of e-banking services to support such clients

- The banks initiative to “migrate” its customers to mobile banking is reflected by its launch of “247 Mobile banking.”

- The efforts by the bank to “migrate” its customers to e-banking are reflected by its provision of e-banking software to its customers.

4.5.4 Customer Care and Operations Strategies

This section was aimed at determining the customer care and satisfaction strategies the bank is using.

- The researcher found that improvements undertaken by the bank to manage customer visits and to “decongest” its branches include:-
  - Investment in information technology infrastructure.
  - Opening of new branches (Over 62 in the first half of 2009).
  - Establishment of branchless banking model that allows its customer's to use any of its 145 branches depending on convenience.
  - Introduction of an expansive ATM network (Over 585 as at the end of June 2009).
  - Introduction of payment cards like Cash back (Over 2,500 service points as at 16th October 2008)
  - Introduction of E-banking
  - Introduction of cell phone banking

4.5.5 Human Resource Strategies

This section was aimed at determining the strength of the bank's human capital.

- What strategies have you put in place to build a competent and motivated workforce?

The researcher noted that the bank has been training its staff in various management courses at leading business schools like Strathmore Business School, IESE Business School and Harvard Business School (Equity Bank Kenya 2008b). In the 2008 financial report the Chief Executive noted that, the bank completed the first phase of its leadership development program where all staff in management positions went through the training.

- What changes have you made on your organizational structure to improve your competitiveness?

  The researcher noted that the bank had expanded the management board by creating positions geared to competitive strategies like Director for Regional Expansion, Director of Leadership Development and Corporate Change, and Director for Corporate Banking (Equity Bank Kenya 2008b).

4.5.6 Other Findings

This section was aimed at gathering any information that would offer more insight on the bank's strategy.

In his presentation of 2009 financial results the Chief Executive presented the bank strategy as:-

- Leveraging on huge capital base to enhance present and future earnings growth,

- Investment in superior technology to
    - allow convergence of banking & telecommunications (MPESA)
    - allow leverage on large customer base to deliver nonbanking services such as custodial, insurance and investment banking services
    - enhance efficiency such as the way 4 switch
    - enhance security such as the EMV (Eurocard Mastercard VISA) technology that reduce credit card frauds
- Regional and national growth to enhance future growth & earnings prospects
    - Southern Sudan
    - Uganda
    - 27 New branches
- Diversification of funding strategy, capital, debt and customer deposits. Allow greater product diversification and stability.
- Optimizing interest earning assets and enhancement of asset quality with emphasis on quality of loan portfolio – improvement in PAR, enhancement of NPL coverage and diversification of loan book to mitigate risk.
- Roll out of an SME strategy; align business with evolving customer needs. Retention strategy for graduating customers becoming acquisition strategy for SME clients.

CHAPTER V: SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary of Findings

Kenyan banks have been forced to develop strategies to help them adapt to the local and global business environment. The objective of this study was to determine which strategies were being utilized by Equity Bank to respond to the competition in the Kenyan banking industry. Currently Equity Bank maintains a strategy similar to the other Kenyan banks although it has been more aggressive in some aspects. The generic strategies have been distribution network expansion, diversification, development of internal resources and infrastructure, and cost management.

The study reveals that the bank had clear strategies to tackle competition in the Kenyan banking industry. This is very encouraging since the essence of competitive strategies is to help organizations to grow and to create sustainable competitive advantages. Among the notable “strategies mix” the bank has been using include product offering diversification, branch and regional expansion, relationship marketing, financing, cost management, customer-care, innovation, and information technology strategies. Due to the successful execution of these strategies the bank has recorded a strong growth in profitability and assets.

The bank has gained varied competitive advantage by application of the various strategic alternatives mentioned above or their mix. Among the dominant strategies observed are financial management, expansion and development of niche markets, mergers and acquisition strategies, development of business infrastructure.

In terms of financial performance Equity Bank, the bank has grown its assets faster than the industrial average. Its profitability has been one of the highest among the listed banks up to 2008. However in 2009 the performance slowed down drastically to a level similar to that of the other leading banks like Cooperative Bank, Kenya Commercial Bank and Barclays. One the assets growth front the competing banks have been closing the gap by listing more shares and issuing bonds. The study also reveals that the competition in the bank industry has increased the level of foreign ownership in the local banks.

On expansion and development of niche markets, Equity bank has built a strong appeal in the last decade that has entrenched it into some niche markets. Some of the niches include micro finance, the industrious kikuyu business community, banc-assurance, and investment banking. The appeals like the "karibu member" advertising campaign have been geared to the mass market. The bank has also started to venture into corporate banking and building an army of marketers to deepen its customer relationship. Development of such relationships would ensure the customers utilize more bank products and are shielded from competition.

Equity bank has been using its expansive nationwide coverage to compete for businesses requiring such networks. It has successfully acquired accounts like CDF (Constituency Development Fund), Women Development Fund, Kenya Power Company, and IPO's. Consolidation through mergers and acquisitions has led to the creation of bigger and more efficient institution in the bank industry. On the expansion from the bank has been successful to make several acquisitions to leverage its growth. However the bank might not have the option for long as its market dominance is bound to make it a focus of the monopoly and competition commission.

The bank hasn't been distributing most of its profits to shareholders but has been aggressively "ploughing" back and aggressively investing the same in developing the business infrastructure. The bank has made heavy investments in branding, information systems and staff development. Branding ensures customer royalty, a reliable workforce enables the bank to develop a reliable and sustained customer satisfaction, and improved information system enables the workforce to be more efficient. Information revolution in the internet and mobile has become a key drive of competition in the bank industry by eliminating some entry barriers and allowing development new products.

5.2 Conclusion

The findings of this study prove the fact that Equity Bank has a well defined strategy being used to compete in the banking industry. The strategies being used by Equity Bank have strong leaning to the blue ocean strategy. The study shows that the strategy being executed by Equity Bank has helped it to outperform its peers. The management of Equity bank has expressed satisfaction with the strategy as it has helped them to grow well so far.

5.3 Limitations of the study

There was lack of response from the bank’s executive directors forcing as to resort to secondary data whose authenticity may be questioned, as it may be have been reported out of context. As secondary data is mainly press communications the interviews may not have given honest answers to the application of the bank’s strategy to protect it and not to be seen as owners of a failed system.

The quoted interviewees weren't required to explain the reason for the responses or statements and therefore to arrive at the conclusions made in the study reference had to be made to the background events and the literature reviewed.

The strategies that had been used by the bank were so diverse that the research had to limit the scope due to limitations of resources.

5.4 Problems encountered

The researcher encountered the problem of the bank's executive director's unwillingness to complete the questionnaires. Some were out rightly reluctant as they felt that their strategy was confidential information. While others kept the questionnaires for weeks only to return them and advising us to refer to the media and their website.

5.5 Recommendations for further research

1. More research is needed to establish the opinion of the line and functional managers towards the bank competition strategies.

2. There seems to be some setbacks with the expansion strategy based on its impact on the profitability; a study needs to be taken to find out why this is the case to help refine the strategy.

3. The study of competition strategy management in the Kenyan bank industry is another area of future research.

4. The study of the impact of the growth of micro businesses to Small and Medium Enterprises (SME's) on the bank competition strategy is another area of future research.

5. There is a need to undertake a research identified by the research have been engraved into the banks corporate culture to ensure sustainability of the competitive strategy.

6. Equity Bank already controls over 50% of the existing bank accounts, research needs to be undertaken to determine whether the bank growth needs to be checked to avoid the creation of a "to big to fail monster" like AIG. This research would be very valuable in determining whether Equity Bank should be allowed to buy out National Bank.

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APPENDIX

A. Letter of Introduction

UNIVERSITY OF NAIROBI

MBA PROGRAMME

TELEPHONE: 4184160/5 EXT. 208 P.O. BOX 30197

TELEGRAMS: “VARSITY”, NAIROBI NAIROBI, KENYA

TELEX: 22095 VARSITY

July 1, 2009

Equity Bank Limited

NHIF Building

Nairobi

Attention: Dr. James Mwangi

Dear Sir,

INTRODUCTION-DEREK ARIEL ABISHUA

The above mentioned is a student of university of Nairobi, pursuing a Masters of Business Administration degree. In partial fulfillment of the requirements for this degree, he is required to carry out a management research project on the real problems in Kenya. His area of study is a case study on Equity Bank strategic responses to competition in the banking industry.

I kindly request you to provide the required information to the best of your knowledge by filling out the attached interview guide. The information is strictly for academic purposes and will be treated in the strictest confidence.

A copy of the research project will be made available to you on request. Your kind assistance will be highly appreciated.

Yours faithfully,

Derek Ariel Abishua John Yabs

RESEARCHER **SUPERVISOR**

B. Interview Guide

This interview guide is being presented to the Chief Executive or his appointed officer at Equity Bank. All data collected will be aggregated, and be kept in a strictly confidence. No individual respondent or organization will be identifiable from any published results. Please complete the form by placing a tick '(?)' in the appropriate box, and by inserting your views where requested. Please return the completed interview guide to the interviewee.

SECTION A: BANK BACKGROUND

1. How many people has your bank employed?

2. How many ethnic communities are included in your payroll?

3. Is your bank using any of the following competitive methods to achieve its strategies?

SECTION B: BUSINESS ACQUISTION STRATEGIES

4. How has the acquisition of businesses assisted you to compete in the bank industry?

5. Why did you prefer to takeover strategy in Uganda instead of start up?

6. What was the main incentive for acquiring Industrial Development Bank "Corporate Bank Division"?

7. What was the main incentive for the acquisition of Housing Finance?

8. What was the main incentive of buying Juanico Investment Bank?

SECTION C: INTERNAL GROWTH STRATEGIES

9. How many branches do you have in Kenya?

10. Has the expansive branch network been useful in your competition strategy?

11. Please name a few advantages of having such a network
    (a)
    (b)
    (c)
    (d)
12. How many of your branches are now profitable?

13. How many branches do you have outside Kenya?

14. In which other countries are you having a presence?

15. Where do you foresee a higher growth? Inside or Outside Kenya

16. In which other countries do you intend to open branches in the next 2 years?

SECTION D: VALUE CHAIN STRATEGIES

17. Which are your main correspondent banks?

18. What is your target market?

19. Do you have a market research or business development unit in your organization?

20. Which are your main sources of revenue/income?

21. How many new products did you introduce in the last 5 years
    (a) Year 2004
    (b) Year 2005
    (c) Year 2006
    (d) Year 2007
    (e) Year 2008
22. What percentage of revenue came from new products last year?

23. Which strategies have we adapted to enable you serve your expansive clientele?

24. Has introduction of new products helped you to beat competition?

25. What is the portfolio mix (percentage wise) of the business sources listed above?

26. What strategies are you using to reach the Kenyan Diaspora?

27. What percentage of CDS custodial accounts do you control?

28. How much business was underwritten by your insurance agency last year.

29. What percentage of your profits is spent on marketing promotion and advertisement? ________

30. How does your ICT system support such a wide clientele without hanging or collapsing?

31. How have you used your ICT system to build a competitive advantage?

32. What strategies have you put in place to build a competent and motivated workforce?

33. What strategy have you adopted to minimize the negative publicity on your bank?

34. What changes have you made on your organizational structure to improve your competitiveness?

35. Which financial strategies has your bank used to compete in the bank industry?

36. How has your financial strength assisted you to compete in the bank industry?

37. What was your average cost of funds in 2008? _________%?

38. What is your dividend policy?

39. Have your retained profits helped you to beat competition?

40. How have you managed to achieve such competitive costs?

41. Has the positioning of your bank as a micro-finance institution helped attract low priced funds or capital from organizations like Africap?

Yes ____ No____ (Tick as appropriate)?

42. How did you manage to get a huge KES 7 billion loan from China?

43. What was the rationale for opting to sell 24.9% to Helios Capital instead of an initial public offering?

44. How do you manage to attract key shareholders like Helios and Africa without losing control?

45. Do you have any shareholders' memorandum of understanding with them?

Yes ____ No____ (Tick as appropriate).

46. Which are five most important improvements undertaken to manage you customer visits and to "decongest" your branches.

(a) -

(b) -

(c) -

(d) -

(e) -

47. What effort have you taken to "migrate" your customers to mobile and e-banking?

48. How do you gather feedback from your customer's?

49. Which of the following best describes the future of competitive strategies in the Kenyan banking industry? Please tick as appropriate. (Key: SD = Strongly Disagree; D = Disagree; A = Agree; SA = Strongly Agree; DK = Don't Know/Neutral)

		SD	D	A	SA	
A	Expansion in number of outlets/production					
B	New product development					
C	Increase marketing effort					
D	Big sales/price cut					
E	Lay off employees.					
F	Better cost control/cut costs					
G	Raise Prices					
H	Improve product quality					
I	Merger and acquisition					
J	Out-sourcing of work					
K	Reduce product range/item					
L	Increase marketing effort					

<u>SECTION E: FURTHER INFORMATION AND CONTACT DETAILS</u>

Please add any specific or general comments on the issues raised in this questionnaire that you feel have not been sufficiently addressed. (Please use more space if it is necessary).

Would you be willing to take part in a short telephone interview to cover specific areas of the survey in more detail?

If Yes, please give your telephone number.

Thank you for taking the time to complete this questionnaire. If you would like to receive a copy of the results, please tick.

Yes Email address

Postal address

If you have any queries about this questionnaire, or if you would like to know more about this research activities please contact researcher at derek.ariel.abishua@gmail.com