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EFFECTS OF RISK MANAGEMENT COMPONENTS ON STRATEGIC IMPLEMENTATION BY COMMERCIAL BANKS IN KISII TOWN, KENYA

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Abstract

Commercial banks and non-banking financial institutions offer corporate and retail banking services but a small number, mainly comprising the larger banks, offer other services including investment banking, insurance services and custodial services among others and thus they ought to take into consideration the implementation of strategy by managing risk. This study evaluates effects of risk management components on strategic implementation by commercial banks in Kisii town. The study adopted an explanatory research design since the study intended to gather quantitative and qualitative data. The target population was 144 employees of nine selected commercial banks existing in Kisii town. The study selected particular staffs including branch managers finance managers, credit managers and subordinates from each commercial *bank. A sample selection of 9 respondents from top level management, 27 respondents from middle level management and 36 respondents from low level management was selected from each bank and thus a sample size of 72 respondents. The study revealed that risk monitoring has a positive impact on strategy implementation among commercial banks in Kisii town. The study found that risk planning had a positive impact on strategy implementation by commercial banks in Kisii town.*

Keywords; Risk Identification, Risk Analysis, Risk Monitoring, Strategic Implementation, Kenya

INTRODUCTION

Risk management from a global point of view is a complex task for any organization and increasingly important in a world where economic events are linked. It is a two-step process. The first is to identify the source of the risk, which is to identify the leading variables causing the risk. The second is to devise methods to quantify the risk using mathematical models, in order to understand the risk profile of the instrument so as to ensure effective strategic implementation (Kealhofer, 2003). From the Regional Perspective strategic implementation involves allocation of sufficient resources financial, personnel, time, and establishing a chain of command or organizational structure, (Balogun & Johnson, 2004). The commercial banks and non-banking financial institutions offer corporate and retail banking services but a small number, mainly comprising the larger banks, offer other services including investment banking, insurance services and custodial services among others and thus they ought to take into consideration the implementation of strategy by managing risk.

Risk management is a structured approach to managing uncertainties through risk assessment, developing strategies to manage it, and mitigation of risk using managerial resources. The strategies include transferring to another party, avoiding the risk, reducing the negative effects of the risk, and accepting some or all of the consequences of a particular risk. The process of risk management is a two-step process. The first is to identify the source of the risk, which is to identify the leading variables causing the risk. The second is to devise methods to quantify the risk using mathematical models, in order to understand the risk profile of the instrument. Credit information sharing can help the banks in identifying the credit risk as well as mitigating the credit risk. There is need for the banks to develop general framework of risk identification and management through credit information sharing and reduce it through debt collection strategies, these techniques can be applied to different situations, products, instruments and institutions. It is crucial for banks to have comprehensive risk management framework as there is a growing realization that sustainable growth critically depends on the development of a comprehensive risk management framework (Greuning and Iqbal, 2007).

Risk management is a complex task for any organization and increasingly important in a world where economic events are linked. It is a two-step process. The first is to identify the source of the risk, which is to identify the leading variables causing the risk. The second is to devise methods to quantify the risk using mathematical models, in order to understand the risk profile of the instrument (Kealhofer, 2006). The techniques of risk identification are facilitative tools intended to maximize the opportunity of identifying all the risks or hazards inherent in a particular facility, system, or product. The tools may be categorized under the broad headings of intuitive, inductive and deductive techniques.

A strategy serves as a vehicle for achieving consistent decision making across different departments and individuals. Hambrick & Cannella (2009) view organizations as composed of many individuals all of whom are engaged in making decisions that must be coordinated. For strategy to provide such coordination it requires that the strategy process act as a communication mechanism within the firm. Such a role is increasingly recognized in the strategic planning processes of large companies. The shift of responsibility of strategic planning from corporate planning departments to line managers and the increased emphasis on discussion the businesses units and the corporate headquarters (as opposed to the formal approval of written plans) are part of this increased emphasis on strategic planning as a process for achieving coordination and consensus within companies (Chakravarthy & White, 2004).

Strategic planning processes are becoming part of companies' knowledge management systems. As management becomes increasingly concerned with how companies create, store, transfer, and deploy knowledge assets, so is strategic planning becoming an integral part of how understanding of the environment is transferred between business units, divisional, and corporate levels and how the knowledge of many different managers and functional experts becomes integrated within strategy (Decoene & Bruggeman, 2006).

Strategy implementation involves allocation of sufficient resources financial, personnel, time, and establishing a chain of command or organizational structure. It involves assigning responsibility of specific tasks or processes to specific individuals or groups. It also involves managing the process. This includes monitoring results, comparing to benchmarks and best practices, evaluating the efficacy and efficiency of the process, controlling for variances, and making adjustments to the process as necessary. Strategy formation and implementation is an on-going, never-ending, integrated process requiring continuous reassessment and reformation (Olson *et al*. 2005). Strategic management is dynamic. It involves a complex pattern of actions and reactions. It is partially planned and partially unplanned. Strategy is planned and emergent, dynamic, and interactive. Strategic management operates on several time scales. Short term strategies involve planning and managing for the present. Long term strategies involve preparing for and preempting the future (Balogun & Johnson, 2004).

In most corporations there are several levels of strategy. Strategic management is the highest in the sense that it is the broadest, applying to all parts of the firm. It gives direction to corporate values, corporate culture, corporate goals, and corporate missions. Under this broad corporate strategy there are often functional or business unit strategies. Functional strategies include marketing strategies, new product development strategies, human resource strategies, financial strategies, legal strategies, and information technology management strategies (Chebat, 2009). The emphasis is on short and medium term plans and is limited to the domain of each department's functional responsibility. Each functional department attempts to do its part in meeting overall corporate objectives, and hence to some extent their strategies are derived from broader corporate strategies (Bourgeois & Brodwin, 2004). Many companies feel that a functional organizational structure is not an efficient way to organize activities so they have reengineered themselves according to processes or strategic business units (SBU). An SBU is treated as an internal profit centre by corporate headquarters. Each SBU is responsible for developing its business strategies, strategies that must be in tune with broader corporate strategies. The "lowest" level of strategy is operational strategy**.** It is very narrow in focus and deals with day-to-day operational activities such as scheduling criteria. It must operate within a budget but is not at liberty to adjust or create that budget. Operational level strategy was encouraged by Drucker (2004) in his theory of Management by Objectives (MBO). Operational level strategies are informed by business level strategies which, in turn, are informed by corporate level strategies.

The Companies Act, the Banking Act, the Central Bank of Kenya Act and the various prudential guidelines issued by the Central Bank of Kenya (CBK), governs the Banking industry in Kenya. The banking sector was liberalised in 1995 and exchange controls lifted. The CBK, which falls under the Minister for Finance's docket, is responsible for formulating and implementing monetary policy and fostering the liquidity, solvency and proper functioning of the financial system. The CBK publishes information on Kenya's commercial banks and non-banking financial institutions, interest rates and other publications and guidelines. The banks have come together under the Kenya Bankers Association (KBA), which serves as a lobby for the banks' interests and addresses issues affecting its members. (Kenya Bankers Association annual Report, 2008).

There are forty-four commercial banks and non-bank financial institutions, fifteen micro finance institutions and forty-eight foreign exchange bureaus in Kenya. Thirty-five of the banks, most of which are small to medium sized, are locally owned (Central Bank of Kenya annual report 2007). The industry is dominated by a few large banks most of which are foreign-owned, though some are partially locally owned. Nine of the major banks are listed on the Nairobi Stock Exchange. In Kisii town there are nineteen commercial banks. The commercial banks and non-banking financial institutions offer corporate and retail banking services but a small number, mainly comprising the larger banks, offer other services including investment banking, insurance services and custodial services among others.

Financial institutions are expected to manage their credit risk to avoid exposing their organizations to unnecessarily high levels of risk and subsequently a decline in performance. Mainly commercial banks create credit due to multiple expansions of banks demand deposits. The banking business is so sensitive because more than 85% of their liability is deposits from depositors used to generate credit for their borrowers, which in fact are a core revenue generating activity for most banks (Saunders and Cornett, 2005). Due to the emerging trends in financial institutions regarding credit risks these may hinder the implementation of strategy in the organizations resulting to under achieving of the overall goals in the longrun. Many organizations are able to generate innovative strategic plans, but few are able to successfully implement these plans.

Some researchers note that organizations fail to implement up to 70% of their strategic initiatives (Miller, 2002).The link between strategy and implementation is complex. The literature suggests that successful strategy implementation is difficult to achieve for six key reasons (Pateman, 2008). These includes persistent pressure from stakeholders for greater profitability, increased complexity of organizations, difficult challenge faced by executives , low levels of participation of a large number of managers across all functions at an early stage of executing strategy, difficulty of securing the required resources to execute the strategy and executives know more about strategy formulation than strategy implementation (Hrebiniak, 2008). A good selection strategy for risk monitoring is adopted by banks implies good pricing of the products in line with the estimated risk which greatly affect their profitability.(Shanmugan and Bourke, 2001).

There is no known study that has been done on the effect of risk management components on strategic implementation by commercial banks in Kisii town; this study therefore seeks to fill the existing research gap. This study was guided by the general and specific objectives. The general objective of the study was to establish effects of risk management components on strategic implementation by commercial banks in Kisii town.

The specific objectives of the study are:

i. To establish the effect of risk identification on strategy implementation by commercial banks in Kisii town.
ii. To establish the effect of risk analysis on strategy implementation by commercial banks in Kisii town.
iii. To investigate the effect of risk monitoring on strategy implementation among commercial banks in Kisii town.
iv. To assess the effect of risk planning on strategy implementation by commercial banks in Kisii town.

THEORETICAL REVIEW

Information Theory

Derban, Binner and Mullineux (2005) recommended that borrowers should be screened especially by banking institutions in form of credit assessment. Collection of reliable information from prospective borrowers becomes critical in accomplishing effective screening as indicated by symmetric information theory which was developed by Claude E. Shannon in 1948. Qualitative and quantitative techniques can be used in assessing the borrowers although one major challenge of using qualitative models is their subjective nature. However according to Derban, Binner and Mullineux (2005), borrowers attributes assessed through qualitative models can be assigned numbers with the sum of the values compared to a threshold. This technique minimizes processing costs, reduces subjective judgments and possible biases. The rating systems will be important if it indicates changes in expected level of credit loan loss. Brown Bridge (2008) concluded that quantitative models make it possible to numerically establish which factors are important in explaining default risk, evaluating the relative degree of importance of the factors, improving the pricing of default risk, screening out bad loan applicants and calculating any reserve needed to meet expected future loan losses.

Seven-S McKinsey Theory

The theory shows that organizational immune systems and the many interconnected variables involved make strategy complex, and that an effective strategy implementation effort must address many of these issues simultaneously. While some models of organizational effectiveness go in and out of fashion, one that has persisted is the McKinsey 7S framework. Developed in the early 1980s by Tom Peters and Robert Waterman, two consultants working at the McKinsey & Company consulting firm, the basic premise of the model is that there are seven internal aspects of an organization that need to be aligned if it is to be successful in strategy implementation so as to ensure proper risk management. The 7S model can be used in a wide variety of situations where an alignment perspective is useful, for example, to help you:

Improve the performance of a company, examine the likely effects of implementing strategy within a company, align departments and processes during a merger or acquisition and determine how best to implement a proposed strategy.

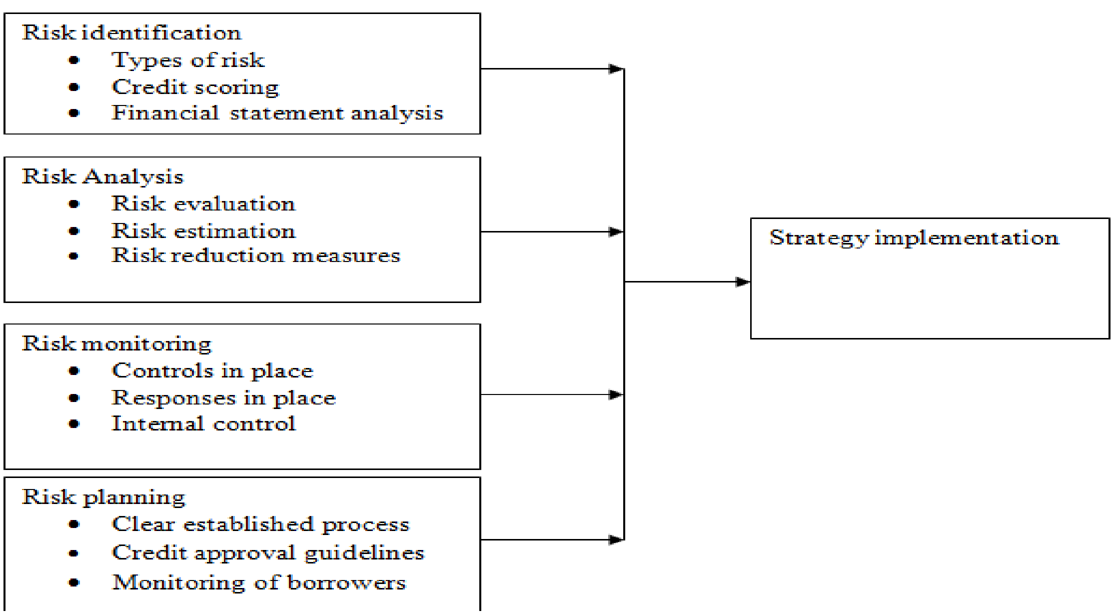
Strategic Triangle Theory

A more interesting alternative is the strategic triangle theory, strategic thinking involves the generation and application of unique business insights to opportunities intended to create competitive advantage for a firm or organization. It involves challenging the assumptions underlying the organization's strategy and value proposition (Kelly *et al.,* 2002). Strategic triangle theory argues that the creation of strategy is the ultimate goal of the organizations and the value proposition that should guide these organizations (Moore, 1995; Moore, 2000). Professor Mark Moore (1995) formulated the Strategic triangle framework to imbue strategic sector managers with a greater understanding of the constraints and opportunities within which they work, and the challenge to create strategically valuable outcomes. His central proposition was that strategy implementation should be effective so as to increase value not only in an economic sense but also more broadly in terms of what is valued by citizens and communities.

Conceptual Framework

The conceptual framework model below shows the various strategy implementation hurdles faced while managing credit risk. These factors (independent variables) need to be credibly addressed in order commercial banks to appropriately implement their strategies.

Figure 1 Conceptual Framework



Research Gap

Locally, Kiptugen (2003) did a study to determine the strategic responses of Kisii town Commercial Bank to a changing competitive environment. Since he focused mainly on strategies that can be adopted in a competitive environment; the study failed to cover the processes involved in strategy implementation and challenges in the implementation phase. Muturi (2005) on the other hand did a study to determine the strategic responses of Commercial banks in Kenya to changes in the external environment. He based his survey on Commercial banks in Kenya. This study focused on a different context and concept from what the current study seeks to cover. Kamanda (2006) also did a study on Kenya Commercial Bank (KCB) with the objective of determining the factors that influence its regional growth strategy. His study, however, does not cover the issues on strategy implementation. Situma (2006) also covered KCB but focused on its turnaround strategy. Muguni (2007) studied the role of executive development in strategy implementation. His was a comparative study of KCB and National Bank of Kenya. These studies fail to capture the process of strategy implementation in relation to risk management. This study sought to establish the effects of risk management components on strategic implementation by commercial banks in Kisii town

RESEARCH METHODOLOGY

This research problem was studied through the use of an explanatory research design. The research focused on effects of risk management components on strategic implementation by commercial banks in Kisii town. The population of this was 144 employees of Commercial banks in Kisii town. The study focused on collecting data from nine selected commercial banks in Kisii town.

Table 1: Target Population

Commercial Bank	Top Level Mgt	Middle Level Mgt	Lower Level Mgt	**Total**
1. National bank Ltd	2	6	8	16
2. Barclays bank ltd	2	6	8	16
3. Diamond trust bank Ltd	2	6	8	16
4. Equity Bank Ltd	2	6	8	16
5. Kenya Commercial Bank Ltd	2	6	8	16
6. Cooperative Bank of Kenya Ltd	2	6	8	16
7. Chase Bank	2	6	8	16
8. Bank of Africa	2	6	8	16
9. Family Bank	2	6	8	16
Total	18	54	72	144

Source: Commercial Banks, HRM Department (2014)

The study selected particular staffs who include branch manager, finance manager and credit manager from each commercial bank since they are the ones conversant with the effects of strategic credit policies on profitability of commercial banks in Kisii town using stratified sampling technique whereby the respondents was stratified into three strata and the respondents picked purposively. The sample size of the study was 72 respondent representing 50% of the entire population. The selection was as follows.

Table 2: Sample Size

COMMERCIAL BANK	SAMPLE SIZE			
	Top Level Mgt	Middle Level Mgt	Lower Level Mgt	**Total**
1. National bank Ltd	1	3	4	8
2. Barclays bank ltd	1	3	4	8
3. Diamond trust bank Ltd	1	3	4	8
4. Equity Bank Ltd	1	3	4	8
5. Kenya Commercial Bank Ltd	1	3	4	8
6. Cooperative Bank of Kenya Ltd	1	3	4	8
7. Chase Bank	1	3	4	8
8. Bank of Africa	1	3	4	8
9. Family Bank	1	3	4	8
Total	9	27	36	72

This study collected both primary and secondary data. With regard to determine effects of risk management components on strategic implementation by commercial banks in Kisii town, the study used a survey questionnaire administered to each member of the sample population. The questionnaire had both open and close-ended questions. The study administered the questionnaire individually to all respondents of the study. The study carried out a pilot study to pretest and validate the questionnaire. Cronbach's alpha methodology, which is based on internal consistency was used. Cronbach's alpha measures the average of measurable items and its correlation. This is in line with a qualitative research design methodology employed in this research proposal. The study selected a pilot group of 10 individuals from the target population to test the reliability of the research instrument.

Inferential statistics was concerned with making predictions or inferences about a population from observations and analyses of a sample. Quantitative data collected was analyzed by the use of inferential statistics and presented through percentages, means, standard deviations and frequencies. The information was displayed by use of bar charts, graphs and pie charts and in prose-form. Content analysis was used to test data that is qualitative in nature or aspect of the data collected from the open ended questions. This study was interested in determine the effects of risk management components on strategic implementation by commercial banks in Kisii town. The study also used Pearson correlation analysis to test the level of significance of the variables on the dependent variable at 95% level of significance.

ANALYSIS & FINDINGS

Descriptive and inferential statistics have been used to discuss the findings of the study. The study targeted a sample size of 72 respondents from which 70 filled in and returned the questionnaires making a response rate of 97.2%, this response rate was satisfactory to make conclusions for the study as Cooper and Schindler (2003), states that a response rate of between 30 to 80% of the total sample size can be used to represent the opinion of the entire population.

Risk Identification

Table 3: Effects of risk identification on Strategy Implementation

Statement	mean	standard deviation
Risk identification is vital for effective risk management	1.91	0.25
Through information sharing among commercial banks can be able to identify various risk the face in lending to the borrower, this will help them in the mitigation of the risk through debt collection or credit sanctions	1.71	0.28
Risk identification is positively significant to influence risk management practices	1.86	0.31
Although the risk exposures of Banks differ and may be complex than conventional financial institution, the principles of credit and market risk management are applicable to both	1.83	0.30

The study sought to determine the extent to which respondents agreed with the above statements relating to risk identification, from the finding majority of the respondents agreed that through information sharing among commercial banks can be able to identify various risk the face in lending to the borrower, this will help them in the mitigation of the risk through debt collection or credit sanctions as shown by a mean of 1.71 and a standard deviation of 0.28, although the risk exposures of banks differ and may be complex than conventional financial institution, the principles of credit and market risk management are applicable to both as shown by mean of 1.83 and a standard deviation of 0.30, risk identification is positively significant to influence risk management practices as shown by mean of 1.86 and a standard deviation of

0.31, risk identification is vital for effective risk management as shown by mean of 1.91 and a standard deviation of 0.25.the above findings concurs with study findings by Sundararajan (2007) he asserts that through information sharing among commercial banks can be able to identify various risk the face in lending to the borrower, this will help them in the mitigation of the risk through debt collection or credit sanctions.

Risk Analysis

Table 4: Statements relating to effects of risk analysis on strategy implementation

Statement	mean	Standard deviation
Credit information sharing among commercial banks can help them in their risk analysis	1.85	0.28
it is useful to classify the different risks according to the amount of damage they possibly cause	1.73	0.27
the application of modern approaches to risk measurement, particularly for credit and overall banking risks is important for banks	1.85	0.28
The need to adopt new measurement approaches is particularly critical for banks because of the role play	1.86	0.29

The study sought to determine the extent to which respondents agreed with the above statements relating to risk analysis, from the finding majority of the respondents strongly agreed that ;risk analysis it is useful to classify the different risks according to the amount of damage they possibly cause as shown by mean of 1.73 and a standard deviation of 0.27,Credit information sharing among commercial banks can help them in their risk analysis, the application of modern approaches to risk measurement, particularly for credit and overall banking risks is important for banks as shown by mean of 1.85 in each case and a standard deviation of 0.28 respectively.

The need to adopt new measurement approaches is particularly critical for banks because of the role play as show by mean of 1.86 and a standard deviation of 0.29, the above findings concurs with the study finding by Sundararajan (2007). Sundararajan that the application of modern approaches to risk measurement, particularly for credit and overall banking risks is important for banks

Risk Monitoring

Table 5: Statements relating to risk monitoring through internal control

Statement	mean	Standard deviation
shareholders of the institutions can use their rights to demand information in order to judge the efficiency of the risk management system	1.83	0.26
Effective risk management requires a reporting and review structure to ensure that risks are effectively identified and assessed and that appropriate controls and responses are in place.	1.76	0.29
Monitoring is the last step in the corporate risk management process	1.80	0.28
Risk monitoring can be used to make sure that risk management practices are in line and proper risk monitoring also helps bank management to discover mistake at early stage	1.80	0.30

The study sought to determine the extent to which respondents agreed with the above statements relating to risk monitoring, from the research findings the study established that majority of the respondents agreed that effective risk management requires a reporting and review structure to ensure that risks are effectively identified and assessed and that appropriate controls and responses are in place as shown by mean of 1.76 and a standard deviation of 0.29, Risk monitoring can be used to make sure that risk management practices are in line and proper risk monitoring also helps bank management to discover mistake at early stage, Monitoring is the last step in the corporate risk management process as shown by a mean of 1.80 in each case and a standard deviation of 0.30 and 0.28 respectively, the finding above concurs with the study findings by Baldoni, (2006), that the area of interest rate risk is the second area of major concern and on-going risk monitoring and is important for banks,

Risk Planning

The study sought to determine the respondent's level of agreement with the below mentioned statements relating to risk planning.

Table 6: Statements relating to risk planning through monitoring of borrowers

Statement	mean	Standard deviation
Strategy selection should be driven by consideration of the type and nature of the risk, manageability and amenability to reduction or control, the degree of severity of impact, available resources and cost-effectiveness	1.75	0.23
Determining strategy first will ensure that responses are aiming for the same goal, and avoid nugatory effort	1.72	0.25
Some risks may require a combination of strategies and multiple responses, whereas others may need only one strategy with a single response	1.78	0.27
selected strategy, can lead to development of tactical responses which target individual risks and aim to realize the strategy	1.75	0.27
Indirect avoidance responses involve doing the project in a different way, which can also eliminate much of the uncertainty by making any impact irrelevant to the project	1.73	0.26
avoidance strategies should be considered as the first option, since it is clearly best to remove risk completely if possible	1.65	0.28

From the research findings the study established that majority of the respondents agreed that avoidance strategies should be considered as the first option, since it is clearly best to remove risk completely if possible as shown by 1.65 and a standard deviation of 0.28,Determining strategy first will ensure that responses are aiming for the same goal, and avoid nugatory effort as shown by a mean of 1.72 and a standard deviation of 0.25,Indirect avoidance responses involve doing the project in a different way, which can also eliminate much of the uncertainty by making any impact irrelevant to the project as shown by a mean of 1.73 and a standard deviation of 0.26, Strategy selection should be driven by consideration of the type and nature of the risk, manageability and amenability to reduction or control, the degree of severity of impact, available resources and cost-effectiveness, selected strategy, can lead to development of tactical responses which target individual risks and aim to realize the strategy as shown by a mean of 1.75 in each case and a standard deviation of 0.23 and 0.27 respectively, Some risks may require a combination of strategies and multiple of 1.78 and a standard deviation of 0.27, the above findings concurs with the findings by (Mwisho, 2001) according to Mwisho (2001), strategy selection should be driven by consideration of the type and nature of the risk, manageability and amenability to reduction or control, the degree of severity of impact, available resources and cost-effectiveness response, whereas others may need only one strategy with a single response as shown by a mean

CONCLUSIONS

From the findings the study established that Risk identification is positively significant to influence risk management practices thus the study concludes that risk identification had positive influence on strategy implementation by commercial banks in Kisii town.

The study established it is useful to classify the different risks according to the amount of damage they possibly cause thus the study concludes that risk analysis had a positive effect on strategy implementation by commercial banks in Kisii town.

The study revealed that risk monitoring can be used to make sure that risk management practices are in line and proper risk monitoring also helps bank management to discover mistake at early stage thus the study concludes that risk monitoring has a positive impact on strategy implementation among commercial banks in Kisii town.

The study found ascertained that determining strategy first will ensure that responses are aiming for the same goal, and avoid nugatory effort thus the study concludes that risk planning had a positive impact on strategy implementation by commercial banks in Kisii town.

RECOMMENDATIONS

Based on the findings, the study recommends that the management on commercial banks should consider adopting risk identification during strategy implementation. This will allow the management to create a comprehensive understanding that can be leveraged to influence stakeholders and create better decisions.

The study also recommends that is very crucial that the organization conducts risk analysis this will help the organization to gather valuable information that will provide valuable insights in the strategy and the necessary input to find effective responses to optimize the risks.

The study recommends that the management keeps on monitoring as well as re-assessing the effect and frequency of mitigation measures adopted. This will help to identify whether the adopted counteractive measures are making any acceptable difference.

The study recommends that the management should have an effective Risk management plan. This will help to identify internal and external risks which are likely to cause a significant increase in the budget, disruption of the schedule or performance problems. By identifying, avoiding and dealing with potential risks in advance, the organization can respond effectively to the challenges whenever they emerge.

It is essential that banks give due consideration to their target market while devising credit risk strategy. The credit procedures should aim to obtain an in-depth understanding of the bank's clients, their credentials & their businesses in order to fully know their customers.

The senior management of the commercial bank should develop and establish credit policies and credit administration procedures as a part of overall credit risk management framework and get those approved from board. Such policies and procedures shall provide guidance to the staff on various types of lending including corporate, SME, consumer, agriculture, etc.

RECOMMENDATIONS FOR FURTHER STUDIES

This research had intended to establish the effects of risk management components on strategic implementation by commercial banks in Kisii town. Other researcher may focus on the relationship between credit risk management and financial performance in commercial in Kenya

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