

**DRIVERS OF COMPETITIVE ADVANTAGE AND PERFORMANCE OF  
COMMERCIAL BANKS IN NAIROBI COUNTY, KENYA**

**BY**

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## DECLARATION

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## **DEDICATION**

This thesis is dedicated to my wife Regina and our daughter Kayla for enduring and according me all support I needed during the period of this study. I also dedicate this to my entire family for supporting me in all areas of life and encouraging me to pursue academic to the highest possible level.

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## OPERATIONAL DEFINITION OF TERMS

<b>Activity Drivers</b>	Support system that enhances effectiveness and efficiency of the banks' activities.
<b>Bank Activities</b>	The main roles and duties carried out by banks towards profit maximizing and to gain competitive advantage.
<b>Commercial Bank</b>	A company which carries on, or proposes to carry on, banking business in Kenya and includes the Co-operative Bank of Kenya Limited but does not include the Central Bank of Kenya.
<b>Competitive Advantage Drivers</b>	Factors within a firm that lead to its gaining and sustaining competitiveness. These influence how a firm gains and maintains a competitive edge and market share within the sector of industry.
<b>Dynamic Capabilities</b>	The firm's ability to integrate, build, and reconfigure internal and external competencies to address rapidly changing environments.
<b>Firm Success</b>	Attaining a competitive position or series of competitive positions that lead to superior and sustainable financial performance.
<b>Intellectual Capital</b>	The knowledge, information, intellectual property and experience that can be put to use to create wealth and/or improve firm performance.
<b>Mobile Banking</b>	A financial transaction conducted by logging on to a bank's website using a mobile device such as a cell phone, including viewing account balances, making transfers between accounts, or paying bills, among others.
<b>Performance</b>	The accomplishment of a given task measured against preset known standards of accuracy, completeness, cost, and speed.

**ABBREVIATIONS AND ACRONYMS**

ATM	Automated Teller Machine
CA	Competitive Advantage
CBK	Central Bank of Kenya
CEO	Chief Executive Office
DC	Dynamic Capability
DCV	Dynamic Capability View
EFTPOS	Electronic Funds Transfer Point of Sale
IC	Intellectual Capital
ICT	Information and Communication Technologies
I&M	Investments and Mortgages
KBA	Kenya Bankers Association
KBV	Knowledge-Based View
KU	Kenyatta University
R&D	Research and Development
RBV	Resource Based View
ROA	Return on Asset
ROE	Return on Equity
SCA	Sustainable Competitive Advantage
VIF	Variance Inflated Factor
VRIN	Valuable, Rare, Inimitable and Non-substitutable

## ABSTRACT

All firms aim at achieving and sustaining competitive advantage, leading to high performance. However, they face challenge on how to achieve and sustain this performance, especially in a rapidly changing environment. Empirical studies indicate that this can be achieved if the firms understand drivers of their competitive advantage. Kenya's commercial banking sector faces such challenges, and though the sector has generally been performing well, there is difference in performance among the banks, with some banks reporting poor performance so far as profit before tax is concerned. This study evaluated the relationship between drivers of competitive advantage and the performance of commercial banks in Kenya. The drivers of competitive advantage studied were bank activities, bank activity drivers, initial conditions and managerial choice. The study also evaluated the moderating effect of dynamic capabilities on the relationship between drivers of competitive advantage and performance. The study was anchored on the Dynamic Capabilities Theory. Explanatory and cross sectional survey designs were employed in the study. The study explored all the 43 commercial banks. Data collection was carried out using a self-administered, semi-structured questionnaire for primary data, whereas secondary data was collected from Central Bank of Kenya website plus the commercial bank websites, with help of a designed tool. The study used descriptive statistics such as mean, standard deviation and percentages, to explain characteristics of data, while inferential statistics, mainly hierarchical multiple regression, were used to test the relationships between drivers of competitive advantage and bank performance. Tables and figures were used to present the results for ease of understanding and interpretation. Statistical package for social sciences (SPSS) was used for analysis. The study established the relationship between performance and bank activities, performance and bank activity drivers, as well as performance and managerial choices, to be positive and statistically significant. Dynamic capabilities were found to have a moderating role between drivers of competitive advantage and performance. However, the study found that initial conditions do not have a significant relationship with performance of commercial banks in Kenya. The study recommends that the banking management lobby for the training of all bank staff on the role and application of the various categories of dynamic capabilities as well as on market volatility and the correct measures to be taken within their banks. The study also recommends that all staff be trained on customer service delivery and customer relationship. Management should also ensure robust training programs involving all their employees so as to uplift their intellectual capital.

# CHAPTER ONE

## INTRODUCTION

### 1.1 Background of the Study

A big question that most researchers and scholars on strategizing wrestle with is why some firms succeed in environments that others fail. This has raised the need to research on the causes of a firm's success and the reason behind differences in the performance of firms within the same industry (Rumelt, 1984; Pavlou, 2011). Just from their literature, early researchers assumed that the nature of the firm and its environment determined success or failure of a firm. However, in these days of globalization and internationalization of markets, competition has become stiffer, forcing firms to strategize and develop better business models to enable them gain and sustain competitive advantage and high performance (Porter, 1980, 1998; Teece, Pisano, & Shuen, 1997).

Another fundamental question in strategic management that has gained attention lately regards the contribution made by dynamic capabilities to performance in dynamic environments (Teece *et al.*, 1997). According to Central Bank of Kenya (CBK), Kenya's commercial bank sector exhibits differences in performance, with some banks reporting very high profits while others report losses before tax on their annual report. This implies difference in performance of firms within a sector that is performing highly in comparison with other sectors and industries within Kenya's economic environment (CBK, 2012).

Feurer (1996), Porter (1998) and Hawass (2010) attributed a firm's success to satisfying three conditions. The first condition was the company's need for development and implementation of an internally consistent set of goals and functional policies that collectively define its market position. This requires a common strategy to coordinate all functions of the business. The second condition is the consistent alignment of the internal set of goals and policies with the firm's strengths, weaknesses, external opportunities and threats. However, in a dynamic environment, the role of strategy is to also maintain a dynamic and not a static balance (Dosi, Nelson, & Winter, 2000; Ambrosini, & Bowman, 2009). The third condition is for the firm's strategy to be mainly focused on the identification and exploitation of its distinctive competencies, the unique strengths that make possible its competitive success. Thus, a firm's attractiveness is viewed as a function of the attractiveness of the industry in which the firm competes and the firm's relative position in that industry.

Each firm has a unique history, organizational culture, capabilities and current policies. These give the firm skills and resources that are critical for success. Every period of time is also unique, as both company and environment are in a state of constant change. However, firms are seen as possessing considerable ability to build on their strengths and overcome their weaknesses to influence or alter their environment and to engineer change over time and not merely respond to it (Porter, 1991, 1998; Ambrosini, Bowman & Collier, 2009).

It's worth noting that some industries perform better than others due to their structures. Thus, some firms may have an attractive position because of their industry. Porter (1991) pointed out that a successful firm is one with an attractive

relative position when an industry structure is held constant. However, there is no single best position in an industry, as the attractiveness of a firm depends on the firm and its initial position. Hence, competitive advantage (CA) may result from a firm's ability to perform the required activities in more unique ways than its rivals or to perform some activities in unique ways that create customer value (Danneels, 2010). According to Porter (1991), a firm's activities can be schematically arranged in value chain and the value system. Arguably, there are some drivers which constitute the underlying source of CA and thus make CA operational.

Competitive advantage can be viewed as any activity that creates superior value above rivals. Hence, a company wants the gap between perceived value and cost of the product to be greater than its competitor's (Ambrosini *et al.*, 2009; Danneels, 2010). Firms may also gain CA through the initial position, managerial choices, resources and the firms' activities (Porter, 1998; Teece, 2007). The strongest competitive advantage is that strategy that cannot be imitated by other companies. For a firm to attain sustainable CA, it has to achieve a superior position, superior skills and superior resources within the industry (Porter, 1998; Wiggs & Ruefli, 2002; Kamukama, Ahiauzu & Ntayi, 2011)

In these days of globalization and internationalization of markets, only firms that have the ability to create and sustain a competitive advantage within the turbulent environment survive (Pavlou, & El Sawy, 2006; Teece, 2006, 2007). This is because environments are rapidly changing, leading to high uncertainty level. This increasing uncertainty may result from higher customer expectations, dilution of borders between competitive environments and the move towards global competition. Once

the firm achieves a sustainable competitive advantage, then the next hurdle is how to gain and sustain high performance (Kraaijenbrink, Spender, & Groen, 2011).

Most successful organizations improve strategy, but they do not often change it outright. New insight into competition and consistent refinement of their ability to implement a stable overall strategy leads to competitive advantage (Porter, 1991; Winter, 2003; Zott, 2003). Competitive advantage may also originate from the ability to make good strategy choices and implement them (Porter, 1991; Kraaijenbrink, *et al.*, 2011). However, the main origin of CA may be found in the firm's proximate or local environment, not lying solely within the firm. The environment shapes how activities are configured, which resources can be assembled in a unique way and what commitments can be made successfully (Porter, 1998).

Firms create and sustain CA by their capacity to continuously improve, innovate, and upgrade over time. Successful firms improve and innovate in valuable ways (Porter, 1991; Teece *et al.*, 1997; Nielsen, 2006). Morecroft (2010) notes that recently there has been an increased interest in the dynamic processes that raise differentiated performance among competing firms. However, there is no standard way of measuring a firm's performance, and some scholars advocate the use of financial ratios while others go for non-financial parameters or a combination of both. This study used a combination of both financial and non-financial measures of performance.

### **1.1.1 Commercial Banks in Kenya**

The commercial bank sector is so critical in most economies that it attracts attention from all circles, including the general public and regulatory authorities. This is because banking institutions perform intermediation functions and consequently influence the level of money through deposit liabilities (Mauri, 1983; Bhatt, 1989; Askari, 1991; Yue, 1992). Hence, it's natural for depositors, investors, regulators and the general public to have vested interest in the performance of banking institutions. Globally, the banking sector has grown as a knowledge sector becoming dynamic and attempting to cope with the competitiveness due to globalisation of economies (Mavridis, 2004). As Gathungu and Mwangi (2012) noted, globalization has accelerated change in innovation-based industries such as banking, finance and information industries.

The banking industry in Kenya is governed by the Companies Act, the Banking Act, the Central Bank of Kenya Act plus the various guidelines issued by the Central Bank of Kenya (CBK) with the aim of introducing prudence in the banking activities. As at 30th June, 2012, the banking sector comprised 43 commercial banks, 1 mortgage finance company, 6 deposit-taking microfinance institutions, 5 representative offices of foreign banks, 115 foreign-exchange bureaus and 2 credit reference bureaus (CBK 2012). Kenyan commercial banks have come together under the Kenya Bankers Association (KBA), which serves as a lobby for the banking sector's interests. KBA serves as a forum for addressing issues affecting member banks, according to Nyangosi (2011). Over the last few years, Kenyan commercial banking sector has continuously grown in assets, deposits, profitability and offered products. This growth is mainly attributed to the industry's wide branch

network in Kenya and in the East African Community region as well as the automation of a large number of services plus the emphasis on addressing diverse customer needs other than just providing the traditional off-the-shelf banking products (CBK, 2012).

During the past few years, players in this sector have experienced increased competition due to increased innovation among the existing players and new entrants into the market. The sector is also contending with new regulations and challenges triggered by the global financial crisis. For instance, the Finance Act 2008 which took effect on 1 January, 2009 that required commercial banks to build a minimum core capital of KShs 1 billion by December, 2012 affected many banks' operation. The global financial crisis that started in 2008 was also expected to affect the banking industry in Kenya, especially in regard to deposit mobilisation, reduction in trade volumes as well as the performance of assets (Nyangosi, 2011).

According to the CBK report for the period ending 30<sup>th</sup> June, 2012, stress tests conducted by the Central Bank indicated that the sector remained sound and resilient. It is worth noting that the financial sector in Kenya is doing better than other sectors and is developing faster than the country's overall economy. For instance, this sector grew by 9.0% in 2010 and 7.8% in 2011, whereas the economy grew by 5.8% and 4.4% in 2010 and 2011 respectively (CBK, 2011, CBK, 2012). The banking sector performance improved in the year 2011, with the sector's profit before tax increasing by 20.4 percent.

The Kenyan banking environment is characterized by different banking products, increased choices, security and accessibility. Thus, the ability of commercial banks

to effectively and efficiently deliver products and services is key to performance and relevance. Over the years, the banking industry has continually introduced a wide range of new products prompted by increased competition, ICT growth and enhanced customer needs. As a marketing strategy, the new products offered assume local brand names to suit the domestic environment in targeting the larger segment of the local customer base (CBK 2012).

Majority of commercial banks in Kenya have added internet banking, mobile phone banking and other products requiring e-banking platform to enhance delivery channels for their customers. However, it is important that the introduction of these products be accompanied with programs to broaden consumer knowledge of the new and more innovative ways of conducting banking business (CBK 2011, 2012). For example, while Internet banking is a fast and convenient mode of conducting banking transactions, it is yet to gain wide acceptance among banking consumers because many potential customers still view this mode of banking with apprehension. Most banks have now partnered with mobile phone service providers to enable their customers use cell phones for mobile banking transactions, including, checking account balances, confirming credit or debit transactions, paying utility bills and transferring funds within and between commercial banks. And in all cases, competitive advantage tends to be in agreement with Porters (1991) drivers of competitive advantage view that superior position, superior skills and superior resources are the main drivers.

According to Barreto (2010), in a turbulent environment, dynamic capabilities (DC) are often considered as the justifying factors for the differentiated success degree of organizations. Therefore, Kenyan commercial banking sector's differentiated

performance might be influenced by dynamic capabilities. It's worth noting that among the different concepts developed so far and employed to justify the different degree of success, Dynamic Capabilities is one of the most recent ones, particularly in a turbulent environment (Zollo & Winter, 2002; Pavlou & El Sawy, 2006; Rai, Patnayakuni & Seth, 2006). The environment in which Kenyan commercial banks operate is turbulent, and this research investigated the role of the factors cited by other scholars.

### **1.1.2 Functions of Commercial Banks in Kenya**

Commercial Banks are generally categorized as a service industry, and their main activities are customer-service oriented. According to CBK (2011), the licensed commercial banks are expected to perform a number of general bank functions. One of the main functions of commercial banks is providing a safe storage for the clients' money. Banks keep the money deposited by customers in vaults. They also undertake to make the money accessible to customers when the latter need it (CBK, 2012). This is done for customers who have accounts with that bank.

The customer accounts are of various types and include current account, personal account, children account, and saving account, to name a few. Commercial banks also facilitate the transfer of money from one account to another. This service comes in handy, particularly for customers wanting to transfer large sums without moving around with the money. The commercial banks facilitate transfer of funds within and across other banks, locally and internationally. This is very convenient for customers (CBK, 2010).

Another important function of banks is offering money lending services. The loans banks give are repaid in installments over a certain period of time that is agreed upon the bank and the borrower during the time of applying for the loan, and they attract interest on the amount borrowed. There are several types of loans, and the rate of interest charged depends on the repayment period and the amount that the customer borrows. Banks also offer financial advice to their customers, for example on the best approach to funding a business start-up (CBK, 2010, 2011). In such cases they provide the customers with the best repayment plan and even business management tips.

Banks offer foreign exchange services also. These include selling foreign currencies to the customers, exchanging foreign currencies for shillings and selling foreign currency to make cross-border payments. This is called foreign currency dealership. Also, foreign suppliers normally want to know the creditworthiness of local importers before they ship the goods and corresponding local banks provide guarantees in form of letters of credit. Thus, banks act as the collateral for the local trader to secure the deal (CBK 2008). The banks also offer their customers investment services. They do this by selling and buying shares of listed companies to the customers or for the customers. Other times they sell their own shares to the customers, offering the latter investment opportunities (CBK, 2009).

Banks act as trustees. They are authorized to manage the property of a deceased person on behalf of the family so that the inheritance wrangles that normally follow one's death do not destroy the business or estate of the deceased. Banks also keep valuable items for customers. These valuables include: title deeds, expensive jewelry among others (CBK, 2012). Like any other services that they offer, they charge a fee

for the safe keeping of valuable items. Banks also offer their customers advice on taxation matters. They guide their customers in preparing tax returns. This is important for customers as it preempts defaulting on taxes and the attendant penalties that can kill a business.

Commercial banks engage in activities such as facilitating payments by telegraphic transfer, EFTPOS, Internet banking, issuing bank drafts and bank cheques. Other functions of commercial banks include accepting money on term deposit, lending money by overdraft, installment loan, and providing documentary and stand-by letters of credit, providing guarantees, performance bonds, securities underwriting commitments and other forms of off-balance sheet exposures (CBK, 2010). Other services include documents and precious items safekeeping, sales, distribution or brokerage, unit trust and similar financial product deals; cash management, merchant banking and private equity financing; underwriting bonds treasury bills and similar credit-related money market securities. However, nowadays most large commercial banks have established a function to handle investment banking (CBK, 2012).

## **1.2 Statement of the Problem**

All firms aim at creating and sustaining competitive advantage and maintaining high performance (Porter, 1998; Pavlou, 2011). However, there are some sectors and industries which perform generally better than others within any given environment, making such industries more attractive. Looking at the Kenyan market, the banking industry is among those industries that are attractive on performance ground. Commercial banks have been performing exceptionally well, reporting positive

profit growth every financial year. For instance, this sector grew by 9.0% in 2010 and 7.8% in 2011, while the national economy grew by 5.8% and 4.4% in 2010 and 2011 respectively (CBK, 2012). The commercial banks sector performance improved in the year 2011, with profit before tax increasing by 20.4 percent.

Firms in high-performing sectors, such as Kenyan commercial banks, are expected to have no performance differentiation. However, this is not the case in Kenya. Some commercial banks have been reporting dismal performance while the sector on average is reporting growth in performance. Table 1.1 gives a summary of the commercial banks reporting poor performance in profit before tax.

**Table 1.1 Percentages of Banks Reporting Negative Profit Before Tax**

Year	Frequency	Percentage (%)
2009	13	30.23
2010	9	20.93
2011	13	30.23
2012	14	32.56
2013	10	23.26

Source CBK, 2014

From Table 1.1 above, its noticeable that the percentage of firms reporting dismal performance is significant and should raise the concern. This is more so because the sector on average has been reporting high performance.

Many scholars argue that performance is influenced by various factors, among them the drivers of competitive advantage (Winter, 2003; Teece, 2007; Jiao, Wei & Cui, 2010). Dynamic capabilities are also believed to positively relate to a firm's long-term performance. Performance is viewed to be the result of a firm's competitive

advantage. However, the studies have not extensively explored the relationship between the drivers of competitive advantage and performance under a dynamic environment. Therefore, there is need to investigate the influence of drivers of competitive advantage on performance and determine whether dynamic capability has any bearing on their relationship. This study sought to investigate the relationship between drivers of competitive advantage and a firm's performance among commercial banks in Kenya.

### **1.3 Research Objectives**

#### **1.3.1 General Objective**

To investigate the effect of drivers of competitive advantage on performance of commercial banks in Kenya.

#### **1.3.2 Specific Objectives**

- i. To determine the influence of bank activities on performance of commercial banks in Kenya.
- ii. To assess the influence of bank activity drivers on performance of commercial banks in Kenya.
- iii. To determine the influence of initial condition on performance of commercial banks in Kenya.
- iv. To determine the influence of managerial choice on performance of commercial banks in Kenya.

- v. To determine the influence of joint effect of drivers of competitive advantage on performance of commercial banks in Kenya
- vi. To determine the moderating effect of dynamic capabilities on the relationship between drivers of competitive advantage and performance of commercial banks in Kenya.

#### **1.4 Research Hypotheses**

This study used the following null hypotheses for the study.

**H<sub>01</sub>**. There is no relationship between bank activities and performance of commercial bank in Kenya.

**H<sub>02</sub>**. There is no relationship between bank activity drivers and performance of commercial bank in Kenya.

**H<sub>03</sub>**. There is no relationship between initial conditions and performance of commercial banks in Kenya.

**H<sub>04</sub>**. There is no relationship between managerial choice and performance of commercial banks in Kenya.

**H<sub>05</sub>**. There is no relationship between joint effect of drivers of competitive advantage and performance of commercial banks in Kenya.

**H<sub>06</sub>**. Dynamic capabilities do not have any moderating effect on the relationship between drivers of competitive advantage and performance of commercial banks in Kenya.

## **1.5 Significance of the Study**

This study aimed at generating knowledge regarding performance of the commercial banks sector in Kenya, especially during the period between the year 2008 and 2012 when, globally, there was an economic downturn. The research investigated the drivers of firm performance in a dynamic environment. This may be of benefit to various categories of interested stakeholders as follows:

### **1.5.1 Scholars and Researchers**

The study adds to the body of knowledge on the area of competitive advantage drivers as well as drivers of commercial banks' performance in a dynamic environment. Since the study was carried out in Kenya, then the findings could be of great help to scholars interested in understanding the various factors influencing commercial banks performance in Kenya. The scholars also may benefit in understanding the relationship of bank activities, bank activity drivers, initial conditions and managerial choice and performance of commercial banks sector in Kenya. Also, the scholar may benefit with the findings of the study regarding the moderating role of dynamic capabilities on the relationship between drivers of competitive advantage and performance of Kenyan commercial bank sector.

### **1.5.2 Policy Makers in Commercial Banks in Kenya**

The study may be of great help to Kenyan commercial banks, as it may help them know how they can enhance and sustain performance. This is of importance especially for the commercial banks operating in rapidly changing environment. The

commercial bank policy makers and strategists can borrow a lot from the study during their policy and strategy development. By exposing the drivers of competitive advantage and their relationship with performance, the study may help the management of commercial banks in strategic allocation of resources and management of their key capabilities and competencies.

### **1.5.3 Government**

The knowledge may also be of help to the Central Bank of Kenya as a government agent. The study may also benefit other government bodies seeking to understand how to survive in the volatile environment with a wide range of quality goods and services to choose from, especially upon the realization of Vision 2030. CBK, on behalf of the government, stands to benefit from the study while carrying out commercial bank supervision by drawing on the study's recommendations to the policy makers.

### **1.6 Scope of the Study**

The study involved all the 43 commercial banks licensed and listed by Central Bank of Kenya as at December 2011 (Appendix G). The study was carried out at the banks' head offices, with the banks' top management as the respondents. The study was carried out within Nairobi County where all the commercial banks have their head offices within central business district and some in the outskirts. This eased accessibility of the target participants during data collection. The study targeted executive officials who would represent their respective commercial banks.

### **1.7 Limitations of the Study**

The Kenya commercial banks sector can be sub-divided into small, medium and large banks based on asset base, but the profits reported differ, with some small banks reporting higher profits than large banks. However, the findings may be assumed to be a reflection of what is generally happening in the entire sector. The study faced challenges of getting the requisite response from the top management of the banks. Nevertheless, the researcher explained the purpose and importance of the study to the bank officials at the banks' head offices. This facilitated booking of appointments with the CEOs' offices for authorization and directions regarding the appointed banks' respondents.

During the data collection period, most of the respondents were reluctant to participate in the survey. The researcher dealt with this challenge by taking more time to explain the agenda and purposes of the study and its possible benefits to the commercial banks in Kenya. Also, the researcher allowed the respondents to take enough time to respond to the questionnaire. This called for the researcher to be patient and persistent despite the inconvenience.

### **1.8 Organization of the Study**

This study is divided into five chapters. The first chapter introduces the subject by giving the background of the study, highlighting the research problem, research objectives and research hypothesis. The first chapter also gives a brief background of the commercial bank sector in Kenya. This laid the foundation of the study on the performance of Kenyan commercial banks. Chapter Two covers the theoretical and

empirical literature review which supports and contributes to the development of this thesis. Various theories on performance are discussed. The research study is anchored to Dynamic Capability Theory and Resource-Based View. The chapter ends with a description of the conceptual framework and an exploration of all the research variables.

Chapter Three focused on the research methodology used for this study. The census and target population are discussed in this chapter. The data collection tools and methodology, data measurement and data analysis tools are also discussed. Chapter Four presents empirical findings and discussion. Results of the study and their analysis are presented in tables and figures for ease of understanding. Chapter Five presents conclusion of the study. It gives a brief overview of the findings, conclusion, policy recommendations and recommendation for further studies.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

This chapter presents literature review on drivers of competitive advantage, dynamic capabilities and firm performance. In addition, the chapter further explores the premise upon which this study is anchored, the theoretical background, the empirical literature as well as conceptual discussion to support the study.

#### **2.2 Theoretical Review**

In search of theories for Sustainable Competitive Advantage (SCA) and firm performance, a number of theories have been raised. This study looks at a few of these theories and highlights their limitations as scholars and researchers continue searching for the best theory. Theories discussed in this study include: Game Theory, Commitment and Uncertainty theory, Resource-based Theory, Knowledge-based Theory and Dynamic Theory.

##### **2.2.1 Game Theory**

Game Theory models seek to explain the equilibrium consequences of patterns of choice by competitors over a variety of strategic variables such as capacity, research and design. These models mainly focus on identifying conditions leading to mutually consistent equilibria and the nature of these equilibria. Each model is

restricted to one or a few variables and assumes that the environment is fixed. For this reason, to determine the outcome, timing plays a key role (Gilbert, 2005). These models are important in helping to understand logical consequences of choices over some important strategy variables. However, by concentrating sequentially on a small number of variables, the models fail to capture the simultaneous choices over many variables that characterize most industries. Also, the models assume many variables as fixed, yet they are known to be dynamic and constantly changing. (Makadok, 2001; Teece, 2007). This theory contributes to the study by explaining the role of managerial choice on firm performance.

### **2.2.2 Commitment and Uncertainty Theory**

Commitment and Uncertainty Theory gives emphasis to the lumpiness of strategy choices and the importance of uncertainty in making them. This assumes that the environment is relatively stable (though in reality it is uncertain) as a result of which commitments have long-term consequences and the possibilities for reconfiguring the value chains limited (Ghemawat, 1991). This approach tends to stress the value of flexibility in dealing with change rather than the capacity to rapidly improve and innovate to nullify or overcome it. The main shortcoming of this theory is that it considers the environment as relatively stable, yet the environment is constantly in a state of flux. The theory also takes into account discrete choices limiting a firm's discretion to shape its environment, respond to environmental changes, or define entirely new positions. This theory supported the Initial Conditions as a driver of competitive advantage.

### 2.2.3 Resource-Based View Theory

Until 1990s, the dominant view in strategic management was that business management was determined by the appeal of the sectors in which the company was competing and by the competitive position of the company in those sectors (Porter & Miller, 1985; Rumelt, 1991; Wiggins & Ruefli, 2002). This gives an external explanation for a firm's competitive advantage capitalizing on the relative imperfections of the sector in which the firm is competing. However, in recent years the idea of analysing a firm's competitive advantage from an intra-organizational perspective based on its own capabilities has made the targeting of business strategies easier (Priem & Butler, 2001; Ray, Barney & Muhanna, 2004).

This intra-organizational focus began to gain general acceptance towards the end of the 1980s and was fully taken on board by firms in the 1990s. It involved a switch towards an introspective search for the origin and explanation of competitive advantage. RBV perspective regards the firm as a unit: a single, organized group of heterogeneous assets that is created, developed, renewed, evolved and improved with the passage of time (Kraaijenbrink, *et al.*, 2011). The acceptance of the concept of the firm as a unit of resources and capabilities prompted interest in identifying the nature of these varying resources and evaluating their potential for profit generation. As DeSarbo, Benedetto and Michael (2007) observes, this heterogeneity in the firm's assets appears to be the central factor in explaining varying performance between firms in the same sector or industry. For this reason, the RBV gives special attention to studying the factors that cause these differences to persist (Mahoney & Pandian, 1992; Amit & Schoemaker, 1993; Grant, 1996; Barney, 2001). However, it failed to evaluate the causes or the process determining these differences.

The logical response to this need has been the interest shown in a new kind of organizational capability, which is the capacity for the self-renewal of resources, routines, capabilities and core competencies (Collis, 1994). This has paved the way for a new asset or highest order, naturally dynamic process, which is the capacity to learn within organizations (individual learning) and learning about the organizations themselves (organizational learning) (Teece *et al.*, 1997; Zollo & Winter, 2002). In this way, dynamic capabilities are formed as a sub-group of the firm's capabilities, allowing the creation of new products and processes, and permitting the company to respond to changing external conditions (DeSarbo, *et al.*, 2007). In this view, it's perceived that dynamic capabilities lead the company to achieve a complex fit between activities that exploit their resources to the full and capabilities that assure good short-term results. Meanwhile, enough resources must be designated for exploration (innovation) to ensure the development of the necessary resources for future strategies and the capacity to adapt to changing external conditions.

The Resource-Based View holds the concept of core competencies and treatments that emphasize intangible assets. This is introspective and centered on the firm itself. This theory argues that firms have unique bundles of resources (Kraaijenbrink, *et al.*, 2011). As a result, they should put effort to address the conditions that allow them to achieve and sustain favorable competitive positions over time. Successful firms are viewed as being the result of their unique resources, which must be nurtured. However, it's known that CA is derived from more than just resources (Carlucci, 2010). RBV views firm resources as intermediate between activities and advantages. RBV have the greatest significance on environments where change is incremental, the number of strategic variables and combinations limited and the time period

ranging from short to intermediate term (Prahalad & Hamel, 1990; Porter, 1991; Priem & Butler, 2001). The theory enriches this study by explaining the achievement and sustainability of CA within firms. This helps in understanding the drivers of competitive advantage under study and their relationship with performance.

#### **2.2.4 Knowledge-Based View Theory**

Knowledge-Based view (KBV) emerged from the RBV and considered knowledge as the key or strategic asset for firms. Knowledge is assumed to be the body or social context in which strategies are developed, sustained and, consequently, protected (Grant, 1996). Therefore, knowledge process and generation is an essential element of analysis to understand strategy development for company evolution and transition (Kogut & Zander, 1992; Orlikowski, 2002; Lei, 2003; Easterby-Smith & Prieto, 2008). However, taking a more dynamic approach, accounting for the processes of learning in uncertainty and dynamic external changes bring about a more realistic analysis and a greater explanatory capacity to a knowledge-based focus.

KBV approach considers firms as bodies generating, integrating and distributing knowledge (Miller, 2002; Easterby-Smith & Prieto, 2008). The ability to create value is based on a set of intangible knowledge-based resources and not as much upon physical or financial resources. As Ranft & Lord (2002) state, to stand a good chance of generating and sustaining high profits, firms must possess stocks of organizational knowledge associated with the creation of value that can be described as uncommon or distinctive. In this perspective, knowledge is considered a key or strategic resource for firms. Hence, it's established as a basic element of analysis

and the processes of generating, developing and applying knowledge assume special importance (Nonaka & Takeuchi, 1995; Nonaka & Konno, 1998).

In the context of an organization, managers play their part in strategic and decision-making roles primarily on the basis of two knowledge-based business assets. These include stocks of knowledge (both of a collective and individual nature), which are resources possessed and controlled by the firm and the dynamic learning processes (collective and individual), which are developed from these stocks of knowledge. These learning processes are business capabilities that are described and studied by different schools of thought as organizational learning (Easterby-Smith & Prieto, 2008). The desired convergence of the KBV and the organizational learning is yet to materialize and they exist as parallel models, the former having economic roots and the latter being more of a sociological nature. According to Pérez-López and Alegre, (2012), the two approaches considerably overlap, working into the same four ontological levels in which organizational learning occurs: individual, group, organizational and inter-organizational.

This theory provides the theoretical understanding of the bank activities as a driver of competitive advantage. Also, this theory supported bank activity drivers and the relationship with performance of the commercial banks. The commercial bank sector is considered a knowledge-based sector and hence this theory played an important role in support of the context of studying the sector.

### **2.2.5 Dynamic Capability View Theory**

This research study attempts to identify some of the existing paradigms in the strategic management field and describe aspects of an emerging new paradigm that is labeled Dynamic Capabilities and link it to performance. During 1980s, the Competitive Forces Approach was the dominant paradigm in the field (Porter, 1980). This approach is rooted in the structure-conduct-performance paradigm of industrial organization and highlights the actions a firm can take to create defensible positions against competitive forces (Mason, 1949; Bain, 1959). A second approach, referred to as Strategic Conflict Approach, is closely related to the first in its focus on product market imperfections, entry deterrence, and strategic interaction (Rumelt, 1995). The Strategic Conflict Approach uses Game Theory tools and consequently implicitly views competitive outcomes as a function of the effectiveness with which firms keep their rivals off balance. This could be through strategies employed in investments, pricing, signaling and control of information. Both the competitive forces and the strategic conflict approaches seem to share the view that rents originate from privileged product market positions (Porter 1980; Prahalad & Hamel, 1990).

Another distinct class of approaches emphasizes building competitive advantage through capturing organizational rents stemming from fundamental firm-level efficiency advantages (Porter & Millar, 1985). These approaches are rooted in discussions of corporate strengths and weaknesses and took a new dimension. This suggests that firms build sustainable competitive advantages only through efficiency and effectiveness. A strand of this literature ('resource-based perspective') emphasizes firm-specific capabilities, firm-specific assets and the existence of

isolating mechanisms as the fundamental determinants of firm performance (Penrose, 1959; Rumelt, 1984; Wemerfelt, 1984). This perspective recognizes but fails to attempt to explain the nature of the isolating mechanisms that enables firm rents and competitive advantage to be sustained.

Teece (2007) developed another component of the efficiency-based showing how rudimentary efforts are made to identify the dimensions of firm-specific capabilities that can be sources of advantage, and to explain how combinations of competencies and resources can be developed, deployed, and protected. This is referred to as the Dynamic Capabilities Approach and stresses exploiting existing internal and external firm-specific competencies in addressing changing environments. This approach emphasizes the development of management capabilities and difficult-to-imitate combinations of organizational, functional and technological skills integrate and draw upon research in such areas as the management of R&D, product and process development, technology transfer, intellectual property, manufacturing, human resources, and organizational learning (Penrose, 1959; Nelson & Winter, 1982; Hayes, Wheelwright & Clark, 1988; Prahalad & Hamel, 1990; Teece, 2007).

According to Teece (2007), the RBV failed to adequately explain the process through which some firms reach positions of competitive advantage in dynamic markets or in situations of change. An approach based on dynamic capabilities endows the basic RBV perspective with a more dynamic nature which emphasizes the strategic value of higher order resources, allowing the generation and renewal of core competencies and competitive advantage (Arend, & Bromiley, 2009; Danneels, 2010). Kraaijenbrink *et al.*, (2011) emphasize that the key role of managers is to appropriately adapt, integrate and reshape organizational skills and resources as well

as internal and external functional competencies. Teece and others (1997) referred the term 'dynamic capabilities' as the firm's ability to integrate, build upon and reconfigure internal and external resources and functional competences to deal with environments which are constantly evolving. Eisenhardt and Martin (2000) argue on similar lines and refer to dynamic capabilities as organizational routines of strategic nature through which firms obtain new configurations of resources when markets emerge, collide, divide, evolve and expire.

Everyday use of the analytical perspective on dynamic capabilities endows strategic processes with greater fluency and rationality as noted by Teece (2007) and Danneels (2010). These processes allow transition between activity and those markets where the firm is already established, as well as provide opportunities they may develop at any time in the future. In this view, a firm is regarded as a continuous, well-ordered flow of dynamic capabilities aimed at attaining strategic objectives and this enables managers to arrive at more balanced decisions affecting aspects such as resources, the firm's activities, present markets and any new opportunities which may arise in the future (March, 1991).

Dynamic Capability View Theory involves longitudinal perspective, allowing investigation of the changes and the continuity in the pattern of organizational behavior over time (Danneels, 2010). During the last decades, there has been an intensive quest for the search of dynamic theory of strategy's detailed longitudinal case studies covering long periods of time because they are necessary for studying these phenomena (Porter, 1991). Dynamic Theory was necessitated by the shortcomings of the Traditional Theory and is developed from three theories; namely, Game theory, Commitment and Uncertainty theory and the Resource-Based

View theory. The theory helps this study to explore the dynamic environment in relation to firm performance.

### **2.3 Empirical Review**

This study aimed at exploring more about how the drivers of competitive advantage influence bank performance as well as the moderating role of dynamic capabilities in that relationship. The study is supported by other scholarly works and studies, some of which are quoted herein. This section looks at the conceptual discussion and then presents a summary of the empirical review.

#### **2.3.1 Performance**

Performance in business is termed as the accomplishment of a given task measured against preset known standards of accuracy, completeness, cost, and speed. It's also the degree to which a feat is being or has been accomplished (Prahalad & Hamel, 1990; Parker, 2000). For instance, the level of success of a salesperson in achieving the monthly goal of fulfilling orders for new customers. It can also be termed as the return provided by an investment or satisfying an obligation. In today's rapidly changing market environment, organizations aiming at high performance must continually evaluate whether their plans and actions are on target and if the organization is designed to successfully implement the necessary plans. According to Nayak and Nahak (2011), in order to survive and succeed, firms need to set strategic directions, establish goals, execute decisions and monitor their state and behavior as they move towards their goal.

According to Cepeda and Vera (2007), once a firm has dynamic capabilities, then it must perform well, and no firm should perform well without dynamic capabilities. Therefore, there is a direct link between dynamic capabilities and performance. On the other hand, some authors link dynamic capabilities to performance, with the assertion that the link is indirect. Zott (2003) argues that dynamic capabilities are indirectly linked to firm performance. This is because dynamic capabilities seek to change a firm's resources, operational routines and competencies and in turn affect economic performance. Similarly, based on RBV, Bowman and Ambrosini (2003), suggest that the VRIN resource base is directly linked to rents, but since dynamic capabilities are one step removed from rent generation, their effect is indirect.

Nevertheless, other scholars have decoupled the notion of dynamic capabilities and performance, arguing that dynamic capabilities do not necessarily lead to competitive advantage (Helfat *et al.*, 2007). They reason that while the dynamic capabilities may change the resource base, this renewal may not necessarily be valuable and may not create any VRIN resources, which means that the new set may either give competitive parity or be irrelevant to the market. Thus, the effect of dynamic capabilities on competitive advantage and performance may be negative. While de-linking dynamic capabilities from competitive advantage, Helfat *et al.*, (2007) suggest that the performance of dynamic capabilities should be evaluated and propose two measures to do so: use of evolutionary fitness (how well the capability enables the firm to make a living by creating, extending, or modifying its resource base); and technical fitness (the quality dimension of capability performance). The latter captures how effectively a capability performs its intended function.

Adaptation of the resource stock of the firm is required even where an essentially stable environment is perceived. Although the rate of change is slow and the extent of change is limited, the requirement for incremental adjustments and improvements to the resource stock of the firm remains important (Ambrosini *et al.*, 2009). Thus, even in stable environments, there is likely to be a need for continuous improvement. However, the resource stock would not be transformed through these change processes but would be incrementally adjusted and adapted. In this relatively stable context, continuous improvement is sufficient to ensure that the resource stock maintains its value. Continuous improvement relates to the continual adjustments that a firm makes to its products or operations (Bessant & Caffyn, 1997).

Incremental dynamic capabilities describes processes that affect changes, albeit incrementally, to the resource base of the firm. This suggests that dynamic capabilities do not only occur in a rapidly changing environment alone but also in more stable market contexts (Eisenhardt & Martin, 2000). Dynamic capabilities are simple and iterative and rely on the incremental and continuous improvement of existing resources. These incremental dynamic capabilities are likely to be repeatable and embedded in the firm (Helfat & Peteraf, 2003; Helfat *et al.*, 2007). Hence, although dynamic capability brings an adaptive change to the resource base, the ways these changes take place do not change.

Renewing dynamic capabilities arise from the incremental DC and this presumed the use of DC to gain SCA in dynamic market environments. These dynamic capabilities are utilized to sustain a rent stream in changing environments. They refresh and renew the nature of the resource stock rather than incrementally adapt it. They are

needed because resource-based advantages in dynamic environments may well be rapidly eroded. If no attempts are made to refresh the resource stock, resource advantages can become disadvantages as the environment shifts (Ambrosini *et al.*, 2009). As Leonard-Barton (1995) explains, valuable resources can become core rigidities if they are not modified, combined with different equipment or extended for new use, such as developing new product lines.

Renewing of dynamic capabilities is not merely about continual incremental changes but is concerned with modifying the resource stock so as to alter its utility, leading to sustained rent generation. It's essential for a firm to continue sustaining dynamic capabilities so as to sustain a resource base that allows earning a rent (Winter, 2003). The cost of sustaining dynamic capabilities is most probably inevitable for any firm in a dynamic environment (Bowman & Ambrosini, 2003). Some firms may try to avoid incurring these costs, but by doing so, they risk being unable to appropriately renew their resource base.

Regenerative dynamic capabilities are likely to be deployed by firms which perceive their environment to be turbulent, where external changes are non-linear and discontinuous (D'Aveni, 1994). As Zahra *et al.*, (2006) explained, firms in volatile environments need to reconfigure their set of valuable resources continually and also need to be able to have the capacity to modify their current dynamic capabilities. The presence of these regenerative dynamic capabilities can be inferred, as it may help explain why some firms find success in the face of environmental turbulence where their competitors fail (Danneels, 2002). Many firms facing a discontinuous environment are not able to overcome their own organizational inertia and thus fail because they have not changed themselves internally (Gilbert, 2005).

The purpose of regenerative dynamic capabilities would be to embed new, or to improve extant, dynamic capabilities (Ambrosini *et al.*, 2009). Like any other dynamic capabilities, regenerative dynamic capabilities come in many forms. These forms might involve restructuring, learning, and leverage. The key distinction is that whereas renewing capabilities operate directly on the resource base, regenerative capabilities impact on the renewing or incremental dynamic capabilities.

### **2.3.2 Bank Activities and Performance**

Consumer behaviour is dynamic and needs to be studied regularly for effective customer service management. As a result of increased awareness, globalisation, deregulation, living standards and urbanization, there has been an increase in the change of preferences, forcing the banking sector to change the features of the products and customer service delivery (Cox & Dale, 2001; Alipour, 2012). The study of consumer behaviour is hence viewed as compulsory in the banking industry so as to keep in touch with the consumers' changing preferences and hence change the products and services offered accordingly. According to Alipour (2012), customers have their own unique needs, demands and preferences in any given segment; thus, banks should study their customers, based on every segment separately. The study of consumer behaviour can enable a bank to tailor its product in such a way as to make it more appealing to the target audience and thus capture the market by giving the bank competitive advantage (Alipour, 2012).

The customer's expectations prior to a service are unique and they influence the customer's evaluation of service performance and satisfaction. Customer service can be divided into high-touch or high-tech services. High-touch services are highly

dependent on the people offering the service, whereas high-tech services are primarily based on the use of automated systems, information technology and other types of physical resources. It's worth noting that high-touch services include also the physical resources and technology-based systems that have to be managed and integrated into the customer service processes (Gronroos, 2001). For instance, electronic banking includes both high-tech and high-touch services. In banking, examples of high-tech services include online banking, mobile banking, ATM machines, among others, while high-touch services consist of instructions and personnel assistance in using the services.

Customer service delivery is differentiable and originates from customers expectations. This necessitates identification and prioritization of expectations for customer service and incorporates these expectations into a customer-service delivery improving process (Kassim & Bojei, 2001). In support, Zeithaml and Bitner (1996) consider content and delivery as two aspects that need to be taken into account when evaluating customer service. However, contemporary factors, like more demanding and informed customers, the emergence of new technologies and the increase in competition modify the relationship between banks and customers, and strategies for survival and business expansion should approach this seriously (Cooke, 1997). As a matter of fact, customers determine the frequency of their contact with banks, based on their previous customer service experiences, and in the long run, this exerts significant impact on the banks' profitability (Bhat, 2005). Once satisfied with service delivery, a customer is less likely to shift to other banks, thus increasing such things as loyalty and retention (Al-Hawari *et al.*, 2005).

Barnes (1997), states that the banking sector seems to be more interested in enhancing a good relationship with customers than with any other industry. However, the increasing deployment of ICT in financial transactions has reduced the physical contact between banks and customers, thus modifying remarkably the general aspect of the relationship. And with the ICT having lowered information costs, customers are able to compare portfolios of investments between banks, or even invest directly (Cooke, 1997).

Another concern when dealing with the customer service in the banking industry is the various issues related to the branches. For instance, access to facilities such as parking lot have a bearing on the mobility of people between the branches; safety and convenience of location make customers access service delivery (Grifell-Tatje & Marques-Gou, 2008). The branches' external and internal architecture may mediate on the perception of service delivery, whereas ATMs inside the branches simplify the customer procedures and lower personnel costs. The number of human attendants is also important and varies according to demand. These are especially useful in reducing time waiting for certain services, providing human interaction and serving elderly and customers who are not technology savvy and thus prefer people instead of machines interfaces for their transactions (Dick, 2003).

Advertising practices and the bank's institutionalized reputation within the community may be related to customer service as well (Dick, 2003). Diversifying the portfolio of services is another strategy for developing a good image within the market. As much as the person who uses many banking services is not likely to move to another bank, sponsoring social activities should also be considered, as this promotes the image of the bank as one that is willing to give back to society.

The role of customers and customer relationships in value creation is accentuated as we move from a production dominated, inside-out, value chain paradigm towards a knowledge-intensive, collaborative value network paradigm where firm boundaries, as well as industry and country boundaries, are becoming increasingly permeable, fuzzy and fleeting (Day, 1994; Dyer & Singh, 1998). Concurrently, the liquification of resources makes reconfigurations of business operations much easier, not only enabling rapid change but also emphasizing that the ability to understand changes in the value network logic and reconfiguring the firm in relation to the network actors will become a competitive advantage (Normann, 2001; Kaj & Suvi, 2009).

Customer relationships can be seen as longitudinal social and economic processes for the co-creation of value (Payne, Storbacka & Flow, 2008). Three main processes are involved in business-to-business customer relationships. These are: customer value-creating process, in which the customer organization applies its capabilities on its resources in a series of activities and management practices to achieve particular goals; firm value-creating process, in which the firm applies its capabilities on its resources in a series of activities and management practices to improve firm performance; and encounter process, in which dyad actors use relational capabilities in collaborative activities and practices of interaction and exchange for the co-creation of value (Woodruff, 1997; Werner, Manfred & Wayne, 2004).

### **2.3.3 Bank Activity Drivers and Performance**

The banking sector in most economies is so critical that it attracts a lot of attention from the public as well as regulatory authorities. According to Mauri (1985), Bhatt (1989), Askari (1991), and Yue (1992), banking institutions perform intermediation

functions and consequently influence the level of money stock through their ability to create deposit liabilities. Therefore, it is critical for depositors, investors, regulators and the public at large to have vested interest in the performance of banking institutions.

Technology, particularly, plays a key role in the financial industry. This has made the banking sector to be among the sectors that have deployed ICT most intensively (Shoebridge, 2005). With the increase of Internet services and cash dispensing machines, the most recurring problems have been mitigated and, in some cases, solved; consequently, the number of customer services increased, making interacting with banks exciting. Of significance is the fact that the new technologies enabled customers to access service in branches other than the branch where their account is (Al-Hawari, Hartley & Ward, 2005).

Information and Communication Technology (ICT) has brought a complete paradigm shift on performance of commercial banks and on customer service delivery in the commercial banks sector. In the present days, ICT has become the heart of the banking sector, as banking industry is considered the heart of every robust economy (Alipour, 2012). ICT has created a new infrastructure for the world economy to become truly global and also provided the users of new technology a competitive advantage over their rivals. Electronic banking system has become the main technology-driven revolution in conducting financial transactions. As banks have made huge investments in telecommunication and electronic systems, users have been encouraged to accept electronic banking system as useful and easy to use (Adesina & Ayo, 2010).

Farrell and Saloner (1985) and Economides and Salop (1992) showed that the embracing of Information and Communication Technology by the banks had two encouraging outcomes. First, ICT can reduce the bank's operational costs. An example is the Internet technology which facilitates and speeds up banking procedures, making it possible and easy to accomplish standardized transactions such as balance enquiries and settlement of bills via online network (Chang-Soo & Lewis, 2004). Second, ICT facilitates and supports transactions between customers within the same network.

The landscape and the dimension of competition in the banking industry have been reshaped by ICT as cited by Aliyu and Tasmin (2012). As a result of the introduction of online banking, ATMs and mobile banking (the initial electronic banking milestones), the diffusion of ICT and increased penetration of Internet have challenged retail banking distribution channels. These include online banking for the delivery of services and products.

Intellectual capital is a fundamental determinant in a firm's current and future competitiveness as well as firm value growth (Wang & Changa, 2005; Magdi, 2008). Tovstiga and Tulugurova (2009) state that the firm's internal resource base is a determining factor of competitive performance, foremost its intellectual capital. Murthy and Mouritsen (2011) observed that competitive advantage is achieved by firms that succeed in mobilizing their intellectual assets in the form of knowledge, technological skills, experience and strategic capabilities. The existing literature further establishes that a firm's competitive advantage and performance are largely influenced by its intellectual capital (Prahalad & Hamel, 1990; Barney, 1991; Tovstiga & Tulugurova, 2009).

Globally, the banking sector has morphed into a knowledge-concentrated sector and has experienced a dynamic and competitive environment due to globalisation of economies (Mavridis, 2004; Gathungu, & Mwangi, 2012). Globalisation has accelerated the need for changes in innovation-focused industries such as banking. The value creation in these industries depends more on intangible assets than physical assets, and these assets are often recognised as IC (Stewart, 1997; Bontis, 1998). The banking sector viewed as a model sector for research on IC issues because the basic nature of its activities is knowledge intensive and the entire banking sector staff are intellectually more identical and consistent than perhaps any other service or business industry in any economy (Kubo & Saka, 2002; Harjinder, 2009).

Employees, also described as human capital, play a crucial role in creating value by increasing efficiency. Through them, firms gain competitive advantage, allowing them to compete in the market (Magdi, 2008; Gathungu & Mwangi, 2012). In sectors such as banking, which rely heavily on knowledge, intellectual capital is thus very important in the process of wealth creation. Mavridis (2004) stated that the nature of the activities of the banking sector is intellectually intensive, so intellectual capital is key to gaining an advantage, which allows them to compete in the market. Individuals working in a firm are considered as strategic competitive resources and are invested on just like tangible assets (Moon & Kym, 2006). Human capital includes knowledge, experience, and special skills of the personnel of a business entity employed in order to create economic value (Cohen & Kaimenakis, 2007). According to Schiuma and Lerro (2008) human capital can be considered as knowledge, skills, intellect, relationship, attitude, talent, and behavior of employees.

Moreover, those resources and assets define the value of the firm from a static point of view and also represent the key critical operative factors to support and drive value creation dynamics over time.

According to Kamukama *et al.*, (2011), intellectual capital promotes a firm's competitive advantage. Intellectual capital encompasses resources and capabilities that are valuable, uncommon, poorly imitable and non-substitutable, which present a lasting competitive advantage and superior performance to the firm (Prahalad & Hamel, 1990; Barney, 1991). Wang and Changa (2005) recognize intellectual capital as a fundamental determinant of a firm's current and future competitiveness as well as firm value growth. Tovstiga and Tulugurova (2009) further affirmed that the firm's internal resource base, foremost its intellectual capital, is a determining factor of competitive performance. Based on their findings, competitive advantage is viewed to be achieved by those firms that succeed in mobilizing their intellectual assets in the form of knowledge, technological skills, experience and strategic capabilities. The existing literature further establishes that the firm's competitive advantage and performance are largely influenced by intellectual capital (Prahalad & Hamel, 1990; Barney, 1991; Tovstiga & Tulugurova, 2009). However, there is need for more empirical research on the practical role of competitive advantage on the relationship between intellectual capital and performance.

#### **2.3.4 Firm Initial Conditions and Performance**

According to Porter (1991), initial conditions influence feasible choices clearly as well as constrain them. Initial conditions may reside within an individual firm or in

its environment. The initial conditions of a firm may include, among others, pre-existing reputation, skills, and activities as a result of its history.

Strategy is not a race to occupy one desired position but a more textured problem in which many positions can be chosen or created. Nevertheless, success requires the choice of a relatively attractive position, given industry structure, firm circumstances and competitors' positions (Porter, 1991). Also, it requires making all the firm's activities consistent with the chosen position. If industry structure is held constant, a successful firm is one with an attractive relative position.

Logistics discipline has adopted capabilities as central to creating and maintaining competitive advantage. Initially, capabilities were described from a relatively static view as unquestionable and lasting over long time periods (Wernerfelt, 1984; Barney, 1991; Grant, 1991; Defee & Fugate, 2010). As the rapidly changing, hypercompetitive, increasingly global supply chain era has shrunk the life of competitive advantages nowadays, the static view of capabilities is swiftly becoming unfeasible (Teece *et al.*, 1997; Eisenhardt & Martin, 2000; Barney, Wright & Ketchen, 2001). Therefore, in order to be competitive in this evolving environment, the creation of dynamic capabilities may be more necessary.

The difference between dynamic capabilities and static or substantive capabilities is that the former provide the means to update and better utilization of existing (static) capabilities and creation of new capabilities (Zahra, Sapienza & Davidsson, 2006). Their use implies that the concept of competitive advantage must move beyond the static view, that presumes that sustainability is the goal, to the dynamic view that considers continuous improvement for short-term advantage to be the only

achievable goal (Teece *et al.*, 1997; Verona & Ravasi, 2003). Effective dynamic capabilities contribute to the race to achieve and maintain long-term competitive advantage by allowing the firm to create a series of temporary advantages and staying one step ahead of competitors (Teece *et al.*, 1997; Eisenhardt & Martin, 2000).

### **2.3.5 Firm Managerial Choice and Performance**

Firms may achieve favourable position and gain competitive advantage through pure managerial choices. These managerial choices, which are made under uncertainty about the future, define the firm's concept for competing, its configuration of activities, and the supporting investments in assets and skills (Porter, 1998). Pure managerial choices lead to the assembly or creation of the particular skills and resources required to carry out new strategies. The skills and market position possessed by any firm today are viewed as the result of past managerial choices about how to configure activities and skills creation or acquisition (Porter, 1991). According to Ghemawat (1991), some of these choices involve hard-to-reverse commitments or path dependency.

As Porter (1991) states, having pools of skills, knowledge, or other resources is not in itself a guarantee of success unless they are the correct ones. Once managers understand their competitive environment and source of their competitive advantages, then they are able to creatively search for favourable positions, assemble the needed skills and assets, configure the value chain appropriately, and put in place supportive organizational routines and culture that reinforces the required internal behavior (Ghemawat, 1991; Porter, 1991).

Strategic capabilities have been described as ‘complex bundles of skills and accumulated knowledge that enable firms to coordinate activities and make use of their assets’ to create economic value and sustain competitive advantage (Day, 1990). Strategic capabilities that are common to businesses can be identified as technological, product development, production process, manufacturing and logistics capabilities. These allow a firm to reduce costs and distinguish its offerings. Increased production efficiency reduces costs, improves consistency in delivery, and ultimately increases competitiveness (Day, 1994).

Market sensing, channel and customer linking, and technology-monitoring capabilities allow a business to respond swiftly to changes in customer needs and to exploit its technological strengths most effectively (Day, 1994). Marketing capabilities, such as skills in segmentation, targeting, pricing, and advertising, allow the firm to take advantage of its market sensing and technological capabilities and implement effective marketing programs (Gathungu, & Mwangi, 2012). Information technology (IT) capabilities enables a firm diffuse market information effectively across all relevant functional areas that can be exploited to direct new product development processes (Nielsen, 2006; Helfat *et al.*, 2007). Management-related capabilities support all of the above and include human resource management, financial management, profit and revenue forecasting, among others.

### **2.3.6 Dynamic Capabilities**

The publication of seminal work on Dynamic Capabilities by Teece, *et al.*, (1997) made the topic one of the most active research areas in the field of strategic management. Moreover, the construct remains open to a variety of

conceptualizations and interpretations in all areas, even its most basic aspects such as definition of dynamic capabilities (Stefano, Peteraf & Verona, 2009). According to Barreto (2010), variation in understanding dynamic capabilities has not only contributed to the richness and vibrancy of the research but also created confusion over the meaning and utility of the construct. This has led some scholars to doubt the existence of dynamic capabilities and view it as just a fanciful concept (Winter, 2003). However, Arend and Bromiley (2009) warn that lack of clarity on basic understanding can hinder fruitful conversation, obstruct progress on the theoretical front, and prevent empirical work from cumulating.

Some researchers have concentrated on the existence of the dynamic capabilities as others attempt to uncover the development and maintenance of such capabilities, as revealed by Barreto (2010). However, dynamic capability is the main construct of interest in dynamic capabilities approach (Stefano, *et al.*, 2009). According to Winter (2003), the importance of an adequate definition of dynamic capabilities for the development of the field could be greater because working with inappropriate constructs would render propositions based on them simply irrelevant. Yet the definition of dynamic capabilities is far from being consolidated.

There has been a lot of debate on the construct of a universal definition of dynamic capabilities. The construct has been criticized for being vague and elusive, mysterious and confusing, abstract and intractable, and obscure and tautological (Winter, 2003; Danneels, 2010). On the other hand, several proposals and findings which deserve full consideration have been provided recently. However, other researchers made new relevant suggestions on definition at the same time. To deal with previous criticisms and incorporate these new theoretical and empirical,

developing a new conceptualization is necessary (Menguc & Auh, 2006; Moliterno & Wiersema, 2007; Pablo, Reay, Dewald, & Casebeer, 2007; Schreyögg & Kliesch-Eberl, 2007; Teece, 2007).

Alternative conceptualizations of dynamic capabilities may vary in terms of the nature, specific role, relevant context, heterogeneity assumptions, and purpose of dynamic capabilities. Barreto, (2010) identified the main challenges associated with each of these dimensions along the existing conceptualizations of the main construct as follows. Dynamic capabilities have been defined as abilities, capacities, processes, and routines in terms of its nature. This poses challenges in making the nature of the construct more specific to avoid the accusations of the field being a “big tent” and non dichotomous to allow varying degrees of dynamic capability across firms, which seems more compatible with real-world situations than a “have it or not” approach. The debate over the basic nature of dynamic capabilities concerns whether it should be defined in terms of latent action, such as an ability, capacity, or enabling device, or in terms of constituent elements, as in a process, routine, or pattern (Stefano *et al.*, 2009). An action that is latent cannot be observed until called into use, while constituent elements have a more concrete and observable form (Helfat *et al.*, 2007).

Early research tended to consider dynamic capabilities as concerning changes in resources, capabilities, operating routines, or one combination of these in terms of its specific role. A number of researchers and scholars considered the central role of dynamic capabilities as related to the change of key internal components of the firm, although the chosen locus of change has varied across elements such as resources and capabilities, operating routines, and resources and routines (Teece *et al.*, 1997;

Eisenhardt & Martin, 2000; Zollo & Winter, 2002; Winter, 2003; Zahra *et al.*, 2006; Helfat *et al.*, 2007). Some studies referred to the concept as a capacity or routines by which an organization alters its resource base (Eisenhardt & Martin, 2000; Helfat *et al.*, 2007). Other researchers looked at it as a two-level hierarchy discriminating between zero-level capabilities and higher-level capabilities (Barreto, 2010). The zero-level capabilities correspond to ordinary capabilities, allowing a firm to make a living in the short term or to substantive capabilities which are used to solve a problem (Winter, 2003; Zahra *et al.*, 2006). In contrast, dynamic capabilities are higher-level capabilities that operate to change ordinary capabilities or substantive capabilities.

Similarly, Zollo and Winter (2002) distinguished two types of routines: operating routines and dynamic capabilities. The operating routines are those employed in the operational activity of the firm while the dynamic capabilities are those dedicated to the modification of operating routines. However, Schreyögg and Kliesch-Eberl (2007) proposed the consideration of capability monitoring a separate organizational function, removed from the operational level and intended to observe both a firm's capabilities usage and evolution and the firm's external environment. Teece (2007) suggested that in addition to the resource reconfiguring capability, two other classes of capabilities should be considered: the capability to sense and shape opportunities and threats and the capability to seize opportunities.

In terms of the relevant context that should be considered, researchers seem divided as to whether to include all or only some of the highly dynamic environments, moderately dynamic environment, or more stable environments. Researchers within the field are divided among those who unequivocally ascribe the concept to highly

dynamic environments, those who accept different degrees of environmental dynamism, those who acknowledge its relevance in both stable and dynamic environments, and those who simply ignore the characteristics of the specific environment (Barreto, 2010). The required link between the existence of dynamic capabilities and the presence of rapidly changing environments is quite clear from the early proposal of Teece *et al.*, (1997). Teece (2007) refined such a link by advocating the special relevance of the concept for environments that are open to international commerce, with systemic technical changes, well developed global markets for goods and services, poorly developed markets for technological and managerial knowledge and when regulatory or institutional shocks occur.

On similar line of thought, Eisenhardt and Martin (2000) argued that dynamic capabilities are not only important in high-velocity markets but also in moderately dynamic markets in which change occurs frequently but along predictable and linear paths. Moreover, they predicted different dynamic capabilities, depending on the firm's market velocity (evident in high-velocity or moderately dynamic markets). In contrast, Zahra *et al.*, (2006) contended that a volatile or changing environment is not a necessary component of a dynamic capability. Corroborating this view, Zollo and Winter (2002) assumed that dynamic capabilities exist and are evident even in environments characterized by lower rates of change.

Concerning the acceptance of dynamic capabilities, some researchers dismiss them as idiosyncratic, whereas others see the existence of significant commonalities among them. Two diverging views can be observed regarding assumptions about a firms' degree of heterogeneity in their dynamic capabilities. Most researchers, particularly those who applied an RBV thinking to this framework, have implicitly

or explicitly assumed that dynamic capabilities are essentially firm specific and unique (Teece *et al.*, 1997; Makadok, 2001). In contrast, Eisenhardt and Martin (2000) asserted that dynamic capabilities exhibit commonalities across firms. They justified the emergence of such commonalities as a result of the existence of multiple, similarly effective ways of performing the task ascribed to the dynamic capability.

According to Barreto (2010), these considerations are not inconsistent with path-dependent processes and imply only that there are multiple paths to achieve the same dynamic capability. Nonetheless, these authors noted that there is no such a thing as a dynamic capability that is exactly alike across firms because such capabilities while showing common features are still idiosyncratic in their details. The corresponding challenge is how to solve the commonalities paradox, that is, how to integrate the existence of commonalities in dynamic capabilities across firms and simultaneously acknowledge the possibility of an impact of dynamic capabilities on performance or competitive advantage.

Some researchers have preferred not to consider its purpose in their conceptualizations, but others have opted to include a purpose associated with the role of dynamic capabilities to make the definition less vague (Easterby-Smith *et al.*, 2009). Those in the latter group are divided regarding whether a specific purpose is required or any purpose will do. Equating dynamic capability with the ability to address rapidly changing environments would raise the criticism of being tautological because of the confusion between the concept and the main proposition that firms with dynamic capabilities are better equipped to deal with changing environments and consequently perform better (Stefano, *et al.*, 2009). However,

requiring that the role be carried out purposefully opens the door to new controversy about the difficulties to empirically test it, either *ex ante* or *ex post* (Barreto, 2010). So, the challenge is to formulate a concept that avoids the specification of a purpose without attracting the criticism of being vague or intractable.

### **2.3.7 Drivers of Competitive Advantage, Dynamic Capabilities and Performance**

It's generally believed that achieving competitive advantage leads to high firm performance. Hence, many firms strive to get competitive advantage, but few truly understand what it is or how to achieve and retain it (Pavlou, & El Sawy, 2006). A competitive advantage can be gained by offering the consumer a greater value than the competitors (Porter, 1990, 1991, 1998). Nonetheless, inimitable strategy is viewed as the strongest competitive advantage. Competitive advantage can also be viewed as any activity that creates superior value over rivals. Most firms gain competitive advantage from new insights into competition and from consistent refinement of their ability to implement a stable overall strategy with its details continually evolving and improving. Ability to make good strategy choices and their implementation is also considered a source of a firm's competitive advantage (Gathungu & Mwangi, 2012). New choices are made from the environmental changes or as accumulating activities and resources open up new options. However, according to Porter (1991), CA may reside in the external environment as much as in an individual firm. The environment shapes how activities are configured, which resources can be assembled uniquely, and what commitments can be made successfully.

Achievement of competitive advantage is not always permanent or even long lasting. As a firm establishes itself in an area of advantage, other firms follow suit in an effort to capitalize on their similarities (Stephan, Tsapin & Talavera, 2012). Therefore, a firm is only said to have a sustainable competitive advantage when its competitors are unable to duplicate the benefits of the firm's strategy. In order for a firm to attain a sustainable competitive advantage, its generic strategy must be grounded in an attribute that meets the following four criteria (Porter, 1998; Barney, 2001). First, it must be valuable, meaning, it should be of value to consumers. Second, it must be rare. This implies that it is not found in common places, or it is not easily obtained. Third, it must be inimitable, meaning, it cannot be easily imitated or copied by competitors. And fourth, it must be non-substitutable, implying that consumers cannot or will not substitute another product or attribute for the one providing the firm with competitive advantage (Porter, 1980, 1998)

Traditionally, the scholars held that CA resides solely inside a company, and competitive success depends primarily on company choices. Currently, an emerging view considers competitive advantage as residing partly in the locations at which company's business units are based and from within the firms (Porter & Siggelkow, 2008). This has resulted in the development of diamond system propagated by Michael Porter (1998). This assumes that a firm's competitiveness is based on constant innovation, relying on four broad attributes: factor conditions: demand conditions; related and supporting industries; and firm structure, strategy, rivalry; and the role of the government.

A firm does not inherit but creates the most important factors of production, such as skilled labor (Porter, 1998). Hence, innovation depends on the rate rather than stock

and efficiency of creating, upgrading and deploying these resources. These factors need to be specific to the industry's particular needs. In regard to Demand Conditions, competitive advantage arises when a firm gets a clear picture of buyers' need from home (Porter, & Siggelkow, 2008). More exacting and sophisticated home demands are better for the firm. The presence of related and supporting industries in the nation, which are internationally competitive, gives relevant dimensions of related industries (Porter, 1998; Porter, & Siggelkow, 2008).

Competitive advantage arises from a combination of management practices, organizational modes favoured in the country and sources of competitive advantage in the industry. Issues such as company goals, management compensation, among others, are considered for firm strategy, structure and rivalry. Strong local rivals stimulate innovation (Porter, 1998; Porter, & Siggelkow, 2008). The government role is considered to be both a catalyst and a challenger for innovation. The government's main tasks includes: promoting rivalry, encouraging change and specializing in factor creation.

Although the environment may provide an initial competitive advantage, the dynamism of the diamond is viewed as the source of sustained competitive advantage. This makes the diamond framework a first attempt to go beyond cross-sectional theories of strategy (Porter & Siggelkow, 2008). The effect of one determinant depends on the others, implying a mutual reinforcement of all determinants. Hence, sustained success depends on the interaction of favourable conditions of determinants, as firms lose competitive advantage due to weakness in their local environment or other internal problem (Porter, & Siggelkow, 2008).

The environment, via diamond, affects the firm's initial conditions and its managerial choices. According to Porter (1998), for firms to achieve competitive advantages, they must understand and exploit their local environment. Thus, there is need for firms to understand better the balance between environmental determinism and company choice in shaping competitive outcome and to understand the degree of stickiness or inertia in competitive positions if a firm stops progressing (Teece *et al.*, 1997).

#### **2.4 Summary of Empirical Literature and Research Gaps**

The following are some studies carried out on the area of dynamic capabilities and firm performance which contributed to the development of this thesis.

Nelson and Winter (1982) noted that dynamic capabilities have greater equifinality, homogeneity, and substitutability across firms than traditional RBV thinking implies. They concluded that effective patterns of dynamic capabilities vary with market dynamism. However, they failed to explain the role of dynamic capabilities in the relation between factors leading to performance and the actual firm performance. Feurer (1996) demonstrated that organizations with dynamic approaches to strategy development achieve superior performance in all competitive environments. Nevertheless, the study did not explicitly use a specific industry or sector, yet different sectors or industries have specific competitive issues or challenges other than market dynamism.

Nielsen (2006) found that dynamic capabilities and the associated knowledge-management activities create flows to and from the firm's stock of knowledge and

they support the creation and use of organizational capabilities. The study suggested that the somewhat elusive concept of dynamic capabilities can be untangled through the use of knowledge-management activities. Therefore, the study suggested that practicing managers who are struggling with the operationalization of dynamic capabilities should instead focus on contributing knowledge-management activities in order to operationalize and utilize the concept of dynamic capabilities. However, the study failed to demonstrate the influence of dynamic capabilities on performance.

According to Salvato (2003), leadership plays a critical role in the evolution of firms and their dynamic capabilities. As Gichunge (2011) found out, administrative and/or legal factors affect both adoption of formal strategic management and organizational performance. Also, the study found out that there is competition to influence adoption of formal strategic management and concluded that organizations with formal strategic management perform better than those without formal strategic management. However, Zajac, Kraatz and Bresser (2000) found the timing, direction, and magnitude of strategic changes to be logically predictable, based on differences in specific environmental forces and organizational resources.

Lee's (2008) study established that a firm's current capability relevance is an important predictor of entry timing with respect to a product market. The study also revealed that entry timing depends upon the dynamics of capability relevance. Hawass's (2010) study indicated that inter-firm collaboration positively relates to the implementation of effective reconfiguration. In addition, the findings revealed that group-level learning is a successful technique for improving a firm's ability to recombine knowledge streams. The study emphasized the role of organization-level

learning in creating the strategic and structural context from which reconfiguration capability operates.

Mugambi, Chege, and K'Obonyo (2011) concluded that market strategy principles have predictive power on corporate performance in Kenya. The findings showed that the predictive power of market principles is significantly enhanced by strategic capabilities. The study revealed that contextual factors do not play a predominant role in predicting corporate performance in Kenya. Kinoti's (2011) study found that policies geared towards increasing the capability to transform R&D activities into commercial innovations would significantly increase the innovative performance of the firms. The findings also found that promotion of in-house R&D and external acquisition of technology positively influenced overall performance of the firms.

Onyango (2011) found that formal education and training are essential in providing basic skills and competencies, and also that on-the-job training in the industry is important for quality production. As Maina (2011) established, the great diversity of small and micro-enterprises affects the impact of intervention in various ways. The study revealed that business growth potential varies with sub-sector and that intervention affects different sectors differently. The study recommended that organizations be assisted to focus their assistance appropriately and propitiously, taking note of the different sub-sector requirements and location dynamics, which mainly determine how assistance is utilized and how it impacts on an enterprise.

**Table 2.1 Summary of Empirical Review and Research Gaps**

<b>Author</b>	<b>Year</b>	<b>Study Title</b>	<b>Findings</b>	<b>Weakness</b>	<b>Gap to Cover</b>
Ayadi,O.F and Omolehinwa, E.	1998	Bank performance measurement in a developing economy; An application of Data Envelop Analysis	Poor management contributes to poor bank performance.	Study was carried out when Nigeria was facing economic challenges and banks were performing poorly.	The study assumed the banks were performance was in a static environment.
Hussain M. and Gunasekaran A.	2002	Management Accounting and Performance measures in Japanese banks	Management Accounting has played a role in measuring performance in different banks in Japan, but its role in measuring Non-financial performance measures has been less significant.	The study was interested in the role of Management Accounting in performance measure and not general performance. The study derived its conclusion from case studies of few banks.	The study assumed banks performance can only be measured financially and thus failed to look at the non-financial performance measures.
Moutinho, L. and Phillips P.A	2002	The impact of strategic planning on the competitiveness, performance and effectiveness of bank branches; A neural network analysis	Overall performance of the branch depends highly on both long term thinking and innovation	Analysis involved 58 managers from 14 branches of 2 banks only. Analysis based on branch performance only.	Study was cried out on banks branches and thus failed to explain performance at corporate level.
Liebach, J and Flohr, J .N.	2003	Customer -focused Technology and Performance in small	Use of customer focused technology leads to high bank's performance	The study is a compares performance between small and large banks.	The study was biased and looked at small and large banks on bases of branch

	and large banks.		network.
Chen M., Cheng S, and Hwang, H. 2005	An empirical investigation of the relationship between intellectual capital and firms' market value and financial performance	Firms' intellectual capital has a positive impact on market value and financial performance, and may be an indicator for future financial performance.	Used financial measures for performance alone and also used the listed companies in Taiwan's stock market.  The study focused on banks registered on Taiwan stock market and failed to include all firms in the sector.
Hsiu-Ling W, Chen C and Shiu F. 2007	The impact of financial development and bank characteristic on the operational performance of commercial banks in the Chinese transitional economy.	The banks performance diminishes with age hence the longer a bank has been in existence, the worse the performance. Small banks had better performance than big banks.	The study used ROA as the main measure of performance. Used only financial ratios as measure of performance.  The study used only ROA to measure financial performance.
Kamath G. B 2007	The intellectual capital performance of Indian banking sector	A vast difference exists in the performance of different segments of Indian banks. Foreign banks perform better than local banks in India	Study used the value added Intellectual coefficient to analyse and rank the banks.  The study was used to rank banks based on intellectual capital only.

Acharya, R.N., Kayan, A. and Lingam, S. R.	2008	Online applications community performance.	banking and bank	The increasing use of online banking has significantly improved the financial performance of community banks.	The study was limited to community bank only and evaluated the influence of online banking to performance alone.	The study was biased towards community banks.
El-Bannany M.	2008	A study of determinants of intellectual capital performance in banks : the UK case		Investment in IT systems, bank efficiency, barrier to entry and efficiency in investment in intellectual capital variables have a significant impact on intellectual capital performance.	The study focused on evaluating factors affecting Intellectual Capital performance and not the banks performance.	The study looked at intellectual performance not corporate performance of the banks.
Grifell-Tatje, E. and Marques-Gou P	2008	Internal performance evaluation: the case of bank branches.		Measure of internal performance (MIP) model can be used as a tool to evaluate branch performance and improve organisational performance.	The tool is branch specific as different branches have different units and roles.	The study focus was banks branches performance and not corporate performance.
Heffernan, T., O'Neill, G., Travaglione, T. and Droulers M.	2008	Relationship marketing: the impact of emotional intelligence and trust on bank performance		There is a significant correlation between trust and financial performance of a relationship manager. Trust is influenced by	Survey was carried out via online and majority respondents were from one major bank. Study concentrated more on trust other than bank performance	Findings were biased towards one large bank.

		knowledge, dependability and expectations.		
Hugkes, J. P. and Mester, L.J. 2008	Efficiency in banking: theory, practice and evidence.	Managerial performance can be explained by agency theory analysed in specific environments	The study dwelled on the theory and what is reported (secondary data) to develop performance model.	The study used only secondary data and theories of performance analysis.
Mahesh, J., Daryll, C. and Jasvinder, S. 2010	Intellectual capital performance in the banking sector: An assessment of Australian owned banks.	VAIC model has a significant relation with human costs and the value addition made by the Australian banks. The size of the bank in term of total assets, total number of employees and total shareholders equity has little or no impact on Intellectual Capital performance.	The sample size is small including only 11 banks owned by Australian and the study left out other key banks in the market owned by foreigners. The study mainly evaluates the impact of IC on value creation other than its direct effect on performance. Study uses only financial ratios as measure of performance.	The study used only state owned banks and used only financial ratios as performance measures.
Mwania, M. and Muganda, N. 2010	An investigation on the relationship between Information Technology (IT) conceptualization and bank performance	Organisations conceptualize IT as means to create impact in its performance. Organisations decision on IT adoption is influenced by industrial pressure.	Study concentrated on IT conceptualization and investment instead of role of IT in influencing performance.	The study did not show how IT influences banks performnce.

			IT implementation is aimed at improving firm performance.		
Deprince, A. E., Ford, W.F. and Morris,P.D.	2011	Some causes of interstate differences in community bank performance.	States' economy, demographic and market structure characteristics explain some of variation in the performance of each state's banks over a given time period.	The study used only ROA as measure of performance.	The study used only ROA as measure of performance.
Murthy, V. and Mouritsen, J.	2011	The performance of Intellectual Capital: Mobilizing relationship between intellectual and financial capital in a bank.	Intellectual and financial capitals complement each other.	The study used case study of one bank to drive conclusion.	The study failed to explain the performance of entire sector since data was collected from only one bank.
Nayak, B. and Nahak, C.	2011	Benchmarking performance of public sector banks in India	Banking sector reform measures have enhanced the efficiency and soundness of the Indian banks and there have been improvement in the performance of many public sector banks in India.	The study concentrated on ranking banks and not on the banking sector performance.	The study analyze more on bench marking banks performance and not on corporate performance

Zou, X. and Huan, T.	2011	A study of the intellectual capital's impact on listed banks' performance in China	Human capital has a positive impact on bank performance.	Study used only the banks listed in China's stock exchange. Performance is measured in terms of technological efficiency.	The study looked at performance only from technology efficiency point of view.
Aliyu A.A, and TASMIN R.B. H	2012	The impact of information and communication technology (ICT) on banks performance and customer service delivery in the banking industry.	Many banks are challenged by the high cost of installing and maintenance of ICT. ICT if well used leads to high bank performance.	The study evaluated ICT influence on performance based on customer service activities. Used only financial measures of performance.	The study analyzed the ICT influence performance indirectly via customer service.
Jelena S and Avelina M	2012	The evaluation of bank performance using a multicriteria decision making model: A case study of Lithuanian commercial banks.	Analytical hierarchy process model is appropriate for using in ranking banks based on their performance.	The study was mainly on ranking banks based on their performance per state and did not capture the sector's performance.	The study developed model to rank banks and not measure their corporate performance.
Stephan, A, Tsapin, A. and Talavera, O.	2012	Main bank power switching costs and firm performance: theory and evidence from Ukraine.	The key determinants of bank switching are bank ownership and foreign affiliation of the main bank. Banks increase loan availability to firms that switch their main banks. Large and more leveraged	The study considered more of the bank's performance and less on the firm that needs to switch the main bank. The study failed to consider the role of regulatory bodies governing bank switching and debts take over.	The study was more on consequences of bank performance other than explaining the factors that influence performance

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		companies are more likely to switch their main banks			
Tan, Y. and Floros, C.	2012	Stock market volatility and bank performance in China	High level of stock market volatility can lead to high performance. Ownership of banks does not have any effect on the performance.	Study used small sample size of only 11 banks. Study evaluated the dynamism in the stock market and not in commercial banks' environment.	The study was more on influence of dynamic capabilities to stock market and not on bank performance.

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**Source Researcher 2014**

## **2.5 Conceptual Framework**

This study adapted a model developed by Porter (1991), which indicated that competitive advantage can be driven by initial conditions, managerial choices, firm activities and firm activity drivers. These are linked to performance, according to the empirical evidence cited in the literature review. The research presumed dynamic capabilities as the moderating variable in the relationship between the independent variables and the dependent variable. The model was summarized and presented in Figure 2.1, highlighting the conceptualized relationship and directions.

The study measured performance using financial and non-financial measures. Financial measures used are ROA, ROE, and profit before tax. Non-financial measures used are: customer base increase, development of new products, growth on branch network and growth on new automated teller machines and sites.

The model presented four dimensions of drivers of competitive advantage. These include bank activities, bank activity drivers, initial conditions and managerial choices. These were individually measured to establish how they influence the bank performance. The model further sought to measure the moderating role of dynamic capabilities. The independent variable was drivers of competitive advantage; the moderating variable was dynamic capabilities; and bank performance was the dependent variable.

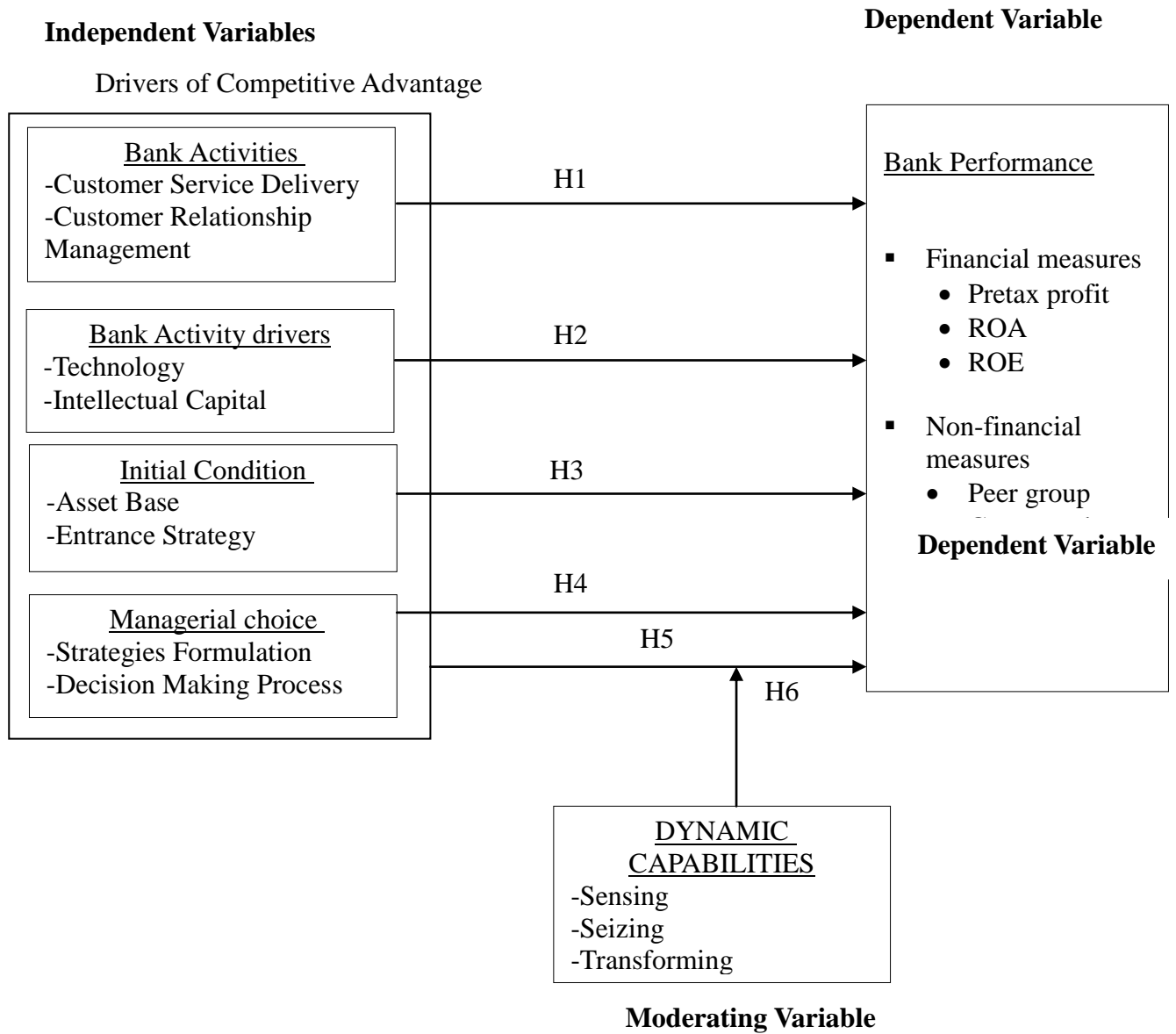


Figure 2.1 Conceptual Framework of the Study

Source: Researcher 2014

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

This chapter provides a description of procedures and methods that were applied in this research. The research was guided by the objectives laid out in Chapter One. This chapter covers the target population, data collection method and instruments, and the data analysis techniques.

#### **3.2 Research Philosophy**

Saunders, Lewis and Thornhill, (2009) posit that the research philosophy considers the role of the assumptions we make about the way the world works; what different philosophies consider as being acceptable knowledge; and the role of our own values and research paradigms. These scholars indicate that research paradigm is a way of examining social phenomena from which a particular way of understanding these phenomena can be achieved and an explanation attempted. This study employed positivism philosophy, which seeks to use existing theory to develop hypotheses that are tested and confirmed wholly, in part, or otherwise refuted, leading to further development of the theory to be tested through further research, according to Saunders et al., (2009)

### **3.3 Research Design**

The study used a mixed design of explanatory and cross-section research design. Explanatory research attempts to clarify why and how there is a relationship between two or more aspects of a situation or phenomenon (Catherine, 2002; Ranjit, 2005). Explanatory research aims at answering the question why. This type of research attempts to go above and beyond exploratory and descriptive research to identify the actual reasons a phenomenon occurs (Kothari, 1985, Kumar, 2005). Explanatory research also attempts to build and elaborate on theories and add to predictions and principles where possible (Kothari, 2009). The study also adopted cross-sectional survey method. The researcher's choice of cross-sectional survey method was prompted by the awareness that it allowed collection of quantitative data from a population in an economical way (Saunders *et al.*, 2009).

### **3.4 Empirical Model**

The study used Multiple Regressions Model. Multiple Regression Equation is considered the appropriate method of analysis when the research involves a single dependent variable presumed to be related to two or more independent variables (Hair, Black, Babin & Anderson, 2010). Multiple regression analysis aims at predicting the changes in the dependent variable in response to changes in independent variables.

Multiple Regression Equation is a technique that can provide both prediction and explanation to the researcher, according to Hair *et al.*, (2010). According to Field (2009), Multiple Regression models require a sample size of between 30 and 100 for

best analytical results. The research target was a population of 43 respondents and thus the Multiple Regression Analysis was fit for data analysis.

To determine the relationship between each independent variable and performance (dependent variable), the research analyses Equations i-iv using Simple Linear Regression. Then to determine the relationship between a combination of all independent variables and the dependent variable, a multiple regression analysis was used on Equation v. Finally, Hierarchical Multiple Regression was used to analyse the effect of the moderating variable using two models on Equation vi.

The research used the following six equations:

Effect of bank activities on performance

$$BP = \alpha + \beta BA + \varepsilon \dots \dots \dots (i)$$

Where  $\alpha$  = model equation intercept

$\beta$  = regression coefficient

$\varepsilon$  = error term

BP = Commercial bank's performance

BA = bank's activities

Effect of bank activity drivers on performance

$$BP = \alpha + \beta BAD + \varepsilon \dots \dots \dots (ii)$$

Where BAD = activity drivers

Effect of initial condition on performance

$$BP = \alpha + \beta IC + \varepsilon \dots \dots \dots (iii)$$

Where IC = initial conditions

Effect of managerial choices on performance

$$BP = \alpha + \beta MC + \varepsilon \dots \dots \dots (iv)$$

Where MC=managerial choices

Overall equation of the effect of Drivers of Competitive Advantage on performance

$$BP = \alpha + \beta BA + \beta BAD + \beta IC + \beta MC + \varepsilon \dots \dots \dots (v)$$

Moderating effect of dynamic capabilities on relationship between drivers of competitive advantage and banks performance

$$\text{Model 1: } BP = \alpha + \beta DCA + \beta DC + \varepsilon$$

$$\text{Model 2: } BP = \alpha + \beta DCA + \beta DC + \beta(DCA * DC) + \varepsilon \dots \dots \dots (vi)$$

Where DC=dynamic capabilities

DCA=drivers of competitive advantage

DCA\*DC = interaction factor

### 3.4.2 Measurement and Operationalisation of Variables

**Table 3.1 Measurement and Operationalisation of Variables**

<b>Variable</b>	<b>Nature</b>	<b>Operationalisation</b>	<b>Measures</b>
Bank performance	Dependent	Bank financial and non financial growth from previous years.	Composite index formed from financial and non-financial performance indicators. The financial data is transformed from ratio to a scale of 1-5 to fit the scale used for non-financial data.
Dynamic Capabilities	Moderator	Special ability for a bank to sense, seize and transform services under management supervision to gain competitive edge.	Dynamic Capabilities = sum of management/ respondent judgements on a scale of 1-5 on sensing, seizing, transforming and managerial capabilities.
Bank Activities	Independent	Customer service delivery and customer relationship management	Customer service delivery= sum of management/ respondent judgements on a scale of 1-5 on customer oriented products and customer satisfaction customer relationship management= sum of management/ respondents judgements on a scale of 1-5 on feedback avenues, queries and complaints response rate and communication
Bank activity drivers	Independent	Intellectual capital and Technology	Intellectual capital =Sum of management/ respondent judgement on a scale of 1-5 on education level, talent development, knowledge management, skill development, and R&D. Technology= Sum of management/ respondent judgements on a scale of 1-5 on IT systems, online services, Internet, Intranet, Mobile Banking
Initial condition	Independent	Initial position, asset base and the entrance strategies used.	Initial conditions = sum of management/ respondent judgements on a scale of 1-5 on initial asset base and the entrance strategies.
Managerial choices	Independent	Strategies process and decision making process.	Managerial choices= sum of management/ respondent judgements on a scale of 1-5 on strategies process and decision-making process.

Source: Researcher, 2014

### 3.5 Study Location

The study was conducted within Nairobi County where all commercial banks have their head offices in different parts of the city. Nairobi is one of the 47 counties in

Kenya and also serves as the capital city. All the commercial banks within Kenya have their head offices in different locations of Nairobi city, with a high concentration of these head offices in Upperhill, Westlands and in the Central Business District (CBD) areas of the county.

### **3.6 Target Population**

The study population comprised all commercial banks licensed and listed by CBK as at 31<sup>st</sup> December 2011. According to CBK 2011 Bank Supervision Annual Report, there were 43 commercial banks. Thus, the total population was 43 commercial banks.

#### **3.6.1 Sampling Design and Procedure**

Saunders *et al.*, (2009) encourage the use of census where the target population is small and within reach for survey studies. Since this target population was only 43 and all respondents were within reach, census design was adopted and therefore there is no need for sampling. The procedure adopted was convenient, as the target respondents were bank's representatives at the head office. Different banks have designated officers who respond on behalf of the bank to public and scholarly research issues. The researcher sought help from each bank's head office for identification of the respondent.

### **3.7 Data Collection Instruments**

The study used semi-structured questionnaires (appendix B) to collect primary data from the respondents. Secondary data was also collected from the various banks as

well as CBK's website. Secondary data was mainly on the bank's financial performance over the last five years. A tool was developed to collect secondary data (appendix C).

### **3.8 Validity and Reliability of Research Instrument**

#### **3.8.1 Validity**

Validity is the strength of conclusions, inferences or propositions. According to Kumar (2005), it is the best available approximation to the truth or falsity of a given inference, proposition or conclusion. Each type of validity highlights a different aspect of the relationship between the treatment (strict attendance policy) and the observed outcome (increased class participation). Validity involves the degree to which one is measuring what is supposed to be measured (the accuracy of your measurement). There are four types of validity commonly examined in social research; namely, conclusion validity, internal validity, constructs validity and external validity (Ranjit, 2005). External validity refers to the ability to generalize the results of study to other settings.

A pilot test was carried out with the commercial banks' branch managers and supervisors within Nairobi city. These were not part of the main study which targeted head offices. A total of 16 respondents participated in the pilot test. The primary purpose of the pilot test was to check face and content validity of the instrument. In addition, the pilot test was used to estimate the average time taken by the respondents to complete the questionnaires. The results of the pilot test assisted in editing and alignment of the research variables to their respective questions. Also,

this enabled eliminate ambiguous words and terminologies in the final questionnaire. A lot of ambiguity was noted in respect of terms used in testing dynamic capability and had to be revised as necessary.

### **3.8.2 Reliability**

Reliability estimates the consistency of measurement or the degree to which an instrument measures the same way each time it is used under the same conditions with the same subjects. Reliability is usually estimated in two ways: test/retest and internal consistency (Hair *et al.*, 2010). Internal consistency estimates reliability by grouping questions in a questionnaire that measures the same concept (Ranjit, 2005). Cronbach's Alpha is a common way of computing correlation values among the questions on an instrument. Cronbach's Alpha splits all the questions on an instrument in all possible ways and computes correlation values for them all. In the end, a computer output generates one number for Cronbach's Alpha. The closer the computed number is to one, the higher the reliability of the estimate of an instrument (Ranjit, 2005).

This research study used internal consistency method to estimate reliability, and the Cronbach's Alpha was computed by determining the manner in which different items of the instrument were related to each other and to the entire instrument. Field (2009) argues that a Cronbach's Alpha value equal or greater than 0.5 is regarded to be an indication of reliability. Therefore, the researcher considered the Alpha coefficient greater than 0.5 to indicate reliability of the research instrument. Table 3.2 presents the results for all the items.

**Table 3.2 Reliability Coefficients of the Research Instrument**

<b>Questionnaire context</b>	<b>Number of Items</b>	<b>Cronbach's Alpha</b>	<b>Comment</b>
Performance	13	0.925	Reliable
Customer service delivery	7	0.909	Reliable
Customer Relationship Management	8	0.897	Reliable
Technology	22	0.951	Reliable
Intellectual Capital	15	0.918	Reliable
Initial condition	8	0.676	Reliable
Managerial choice	6	0.51	Reliable
Sensing dynamic capabilities	4	0.923	Reliable
Seizing dynamic capabilities	4	0.815	Reliable
Transforming dynamic capabilities	4	0.89	Reliable
<b>Over all</b>	<b>91</b>	<b>0.969</b>	<b>Reliable</b>

Source: pilot study 2014

The entire instrument was reliable, with Cronbach's Alpha of 0.969. However, managerial choices had a low reliability, with Cronbach's Alpha of 0.510, while Initial Conditions were moderately reliable, with Cronbach's Alpha of 0.676. The rest had high reliability, with Cronbach's Alpha of above 0.8. Technology had the highest Cronbach's Alpha of 0.951, followed by Performance, with Cronbach's Alpha of 0.925. Cooper and Schindler (2007) indicate that for an instrument to be regarded as reliable, the value of Cronbach's Alpha coefficient has to be at least 0.5. Thus, the instrument was considered to be reliable for carrying out the survey.

### **3.9 Data Collection Procedures**

Before collecting data, the researcher got authorization from Kenyatta University Graduate School and the Ministry of Higher Education, under the National Commission for Science, Technology Research and Innovation (Appendix H). The

researcher was issued with research permit number NACOSTI/P/14/1442/3544 by the National Commission for Science, Technology, Research and Innovation. Also, the researcher sought approval from the various commercial bank CEO's offices from where directions were given to the respondents. The questionnaires were delivered to the respondents and collected later to increase the chances of a higher rate of response. Secondary data was collected using a developed data collection tool from CBK's Bank Supervision Annual Report. Data collection was done from the month of October to December 2014.

### **3.10 Data Analysis and Presentation**

The main aim of this process is to assemble or construct data in a meaningful or comprehensible fashion. Yin (1994) observes that data analysis consists of examining, categorizing, tabulating or recombining the evidence to address the initial propositions of a study. Once the questionnaires were received back, they were screened and edited to remove deficient, incoherent and erroneous responses. The study used descriptive statistics for the analysis of the data characteristics and presented results using tables and figures. The frequencies, mean, standard deviations and percentages were used to interpret the information. Exploratory Factor Analysis was used to identify constructs and develop composite indices for all variables which were used for the inferential statistic analysis. Then simple and multiple and hierarchical multiple regressions were run on SPSS Version 20 for inferential statistic analysis. The various analyses carried out using the SPSS were presented and discussed.

### **3.10.1 Diagnostic Tests Normality of Data**

#### **a. Normality Test**

Statistical methods are based on various underlying assumptions. One common assumption is that a random variable is normally distributed. When this assumption is violated, interpretation and inference may not be reliable or valid. Statistical tests for normality are more precise since actual probabilities are calculated. The Kolmogorov-Smirnov and Shapiro-Wilks tests for normality calculate the probability when the sample was drawn from a normal population.

The hypotheses used are:

$H_0$ : The sample data is not different from a normal population.

$H_a$ : The sample data is different from a normal population.

This study used Shapiro-Wilks Test, which works best for data sets with  $n < 200$  (Field, 2009). The Shapiro-Wilk is the ratio of the best estimator of the variance to the usual corrected sum of squares estimator of the variance (Shapiro & Wilk, 1965). The statistic is positive and less than or equal to one. Being close to one indicates normality. This test was run using SPSS analytical program.

#### **b. Linearity Test**

Multiple Regression can only accurately estimate the relationship between dependent and independent variables if the relationships are linear in nature (Tabachnick & Fidell, 2001). Linearity means that the amount of change or rate of change between scores on two variables is constant for the entire range of scores for the variables. Linearity can be evaluated using graphical or statistical methods. Graphical methods include the examination of scatter plots, often overlaid with a

trend line. Statistical methods include Linear Correlation Coefficient (Gupta, 2010). If the relationship between independent variables (IV) and the dependent variable (DV) is not linear, the results of the regression analysis will underestimate the true relationship. This underestimation carries two risks: increased chance of a Type II error for that IV, and, in the case of multiple regression, an increased risk of Type I errors, that is, over-estimation of other IVs that share variance with that IV (Field, 2009)

This study adopted Linear Correlation Coefficient to test for linearity and confirmed the linear relationship using the positive direction plus the strength of the coefficients as well as the significant level of the relationship.

### **c. Multi-collinearity Test**

Multi-collinearity refers to a situation in which two or more explanatory variables in a multiple regression model are highly linearly related. A perfect multi-collinearity occurs if the correlation between two independent variables is equal to 1 or -1 (O'Brien, 2007). Multi-collinearity can be detected using tolerance or the variance inflation factor (VIF). A tolerance of less than 0.20 or 0.10 and/or a VIF of 5 or 10 and above indicates a multi-collinearity problem. According to Belsley (1991), existence of multi-collinearity may lead to Type II error. The study used SPSS to check for multi-collinearity, with a threshold tolerance of 0.2 and VIF of 10.

### **3.11 Research Ethics**

The main ethical issues in this study revolved around confidentiality and honesty among participants as well as data collection in general. The researcher addressed these key

ethical concerns in the best possible way. Confidentiality concerned mainly the identity of the commercial banks. All the participating banks granted the researcher access to their appointed respondent, but preferred not to be identified by name, given the highly competitive nature of the banking industry, compelling the researcher to describe the firms in a general manner. Honesty among the research participants was necessary for the success of this study. For this reason, the researcher insisted on honesty on the part of all of the respondents. This was necessary, since not all participants may have been aware of what constitutes ethical behavior. According to Zickmund & Babin, (2010), honest cooperation is the main obligation of the research participant. Concerning data collection, the researcher sought permission from the head offices of all commercial banks, upon explaining the nature and objective of the study before delivering the questionnaires. The purpose of this was to encourage participation.

## CHAPTER FOUR

### EMPIRICAL RESEARCH FINDINGS AND DISCUSSION

#### 4.1 Introduction

This chapter presents the results and discussion of the study conducted to determine the relationship between initial conditions, managerial choices, bank activities, bank activity drivers, dynamic capabilities and performance of commercial banks in Kenya. The chapter covers response rate, demographic characteristics of respondents, descriptive and inferential statistics of the study variables.

#### 4.2 Response Rate

The researcher distributed 43 questionnaires to the respondents. However, only 40 questionnaires were considered usable for the analysis. Table 4.1 presents results of the response rate.

**Table 4.1 Response Rate of the Census**

Responses	Frequency	Percentage
Completed usable questionnaires	40	93.02%
Unusable, unreturned and disqualified questionnaires	3	6.98%
<b>Total</b>	<b>43</b>	<b>100%</b>

Source: survey data 2014

The researcher issued 43 questionnaires (one questionnaire per commercial bank), out of which 41 were received back. One questionnaire was disqualified due to

incompleteness, thus 40 questionnaires were considered as suitable for the analysis. This translated to 93.02% of the targeted total of 43 questionnaires. According to Saunders *et al.*, (2009), a response rate of 50 percent is adequate, 60 percent good and a response rate of 70 percent and above considered very good. Therefore, the response rate of 93.02% achieved was adequate for drawing conclusions on the study objectives.

### 4.3 Descriptive Statistic Analysis

#### 4.3.1 Descriptive Analysis for Performance

To understand the banks' view on performance, the respondents were asked to rate their bank's views on various performance factors. The responses were on a scale of 1-5, where 1=below average, 2=average, 3=above average, 4=good, and 5=excellent. The percentages, mean and standard, were computed as presented in Table 4.2

**Table 4.2 Results of Performance Rating**

Statement	N	Min	Max	Mean	Std. Deviation
Overall performance	40	1	5	4.03	.800
Profit before tax	40	1	5	3.80	.966
Profit after tax	40	1	5	3.75	.981
Return on investment	40	1	5	3.93	.944
Return on assets	40	1	5	3.88	.883
Return on equity	40	1	5	3.80	.883
Customer base growth	40	1	5	3.68	1.071
Development of new products	40	1	5	3.90	1.008
Adoption and application of new technology	40	1	5	4.18	.903
Innovation	40	1	5	3.78	1.000
Staff retention within the bank	40	1	5	3.40	1.057
Opening new branches	40	1	5	3.58	1.174
New ATM machines and sites	40	1	5	3.38	1.390
<b>Aggregate score</b>				<b>3.77</b>	<b>1.005</b>

Source: Survey Data 2014

A mean score of 3.77 and SD of 1.01 indicate that majority of the respondents view their banks' performance to be above average. Overall performance was rated, with high M=4.03, SD=.80 where 5% rated average, 15%, above average, 52.5% good and 27.5% excellent performance. In regard to setting up of new ATM machines and sites, the ratings were: 10% below average, 20% average, 25% above average, 12.5% good, and 32.5% excellent. The mean score was 3.38 and SD 1.39. This indicates that various banks view the effect of the addition of ATM service differently and many do not consider it as giving a competitive edge. Unstructured interview revealed that this is due to the new banking mode of agency banking, which many banks are adopting at the expense of ATM, while others use universal ATM machines, outsourced as a way of reducing operational cost and risk. Return-on-investment was rated as excellent at 30%, good at 42.5 %, above average at 17.5%, average at 30%. None of the respondents rated it as below average. The mean was 3.93 and SD .944, implying a high mean and moderate SD. This indicates that the banking industry is performing well by shareholders' equity returns.

The results were in agreement with the secondary data collected from CBK and various bank websites and the information used to analyse performance of the commercial bank sector for the last five years (2008-2013). As recommended by Moutinho and Phillips, (2002); El-bannany (2008); and Jehena and Avelina (2012), both financial and non-financial measures of performance were applied to analyse the sector's performance for best results to be obtained. Market share categorization and growth of customer base were used to evaluate non-financial performance, while profit before tax, ROA and ROE, were used to evaluate financial performance.

The results indicated a performance growth by both measures (financial and non-financial) for the entire sector.

The secondary data revealed that commercial banks in Kenya are grouped under three categories: small, medium and large, based on the market share. A bank with market share below 1% is labeled 'small'; one with a market share bigger than 1% but less than 5% is labeled 'medium'; and one with a market share above 5% is labeled 'large'. The market share index used is a computed composite of net assets, deposits, capital, number of loan accounts and number of deposit accounts (CBK, 2013). Out of the 43 commercial banks, 6 are categorized as large, 15 as medium and the rest 21 as small. Table E (appended) gives full list and grouping of each individual bank for the last five years. During the last five years, only Guaranty Trust Bank Ltd and Ecobank Kenya have made a significant impact on their market share. Ecobank did poorly and went lower, from medium to small, whereas Guaranty Trust bank improved and was promoted to medium from small.

The customer base growth indicates that the entire sector grew by 28.97% in 2009, 2,064.4% in 2010, 16.78% in 2011, 83.42% in 2012 and 21.94% in 2013. A detailed growth analysis per individual bank is in Table F in Appendices Section. Therefore, we can conclude that the sector is doing well on customer base growth. However, as Teece (2006) warns, customer preferences and needs keep on changing and thus banks require dynamic capabilities to retain the consistent growth over time. These results were in support of the research survey finding indicating an above-average performance with mean= 3.68 and SD= 1.07

Over the last five years (2008-2013), the sector has reported high profit, indicating good financial performance (appendix G1). The computed results from secondary data indicated that the sector's growth was 12.7% in 2009, 50.6% in 2010, 19.5% in 2011, 20.5% in 2012 and 16.1% in 2013. This supports the research survey results which reported a mean of 3.80 and a SD.966

The secondary data collected indicated that there has been a positive growth on ROE in the entire commercial bank sector in Kenya (appendix G3). The computed result, excluding one bank which had not posted reports, showed a positive growth over the last five years. The sector exhibited growth of 13.73% in 2009, 20.46% in 2010, 21.12% in 2011, 15.46% in 2012, and 19.45% in 2013. This is in agreement with the research findings where ROE was rated high, with a mean of 3.80 and SD of 0.883.

#### **4.3.7 Bank Activities**

The respondents were required to indicate their banks' position rating on the bank activities on a scale of 1-5, where 1 = below average, 2= average, 3= above average, 4= good, and 5= excellent. The results computed are as presented in Table 4.3

**Table 4.3 Results of Bank Activities Rating by Respondents**

Statement	N	Min	Max	Mean	Std. Deviation
The bank provides customers the services as promised.	40	1	5	4.18	0.781
The bank provides accurate service to customers	40	1	5	4.03	0.8
The bank honors its commitments.	40	1	5	4.23	0.733
Bank staffs are knowledgeable to solve customers' problems.	40	1	5	4.05	0.815
Staff have the enthusiasm to understand customer needs	40	1	5	3.95	0.904
Staffs consider customer needs in the first place.	40	1	5	4.13	0.822
Staff can provide customers precise personal services	40	1	5	3.9	1.057
The bank ensures security of customers during the transaction process	40	1	5	4.55	0.552
The bank provides quality services, increasing the customers' confident and trust.	40	1	5	4.2	0.723
Bank staffs provide customers with prompt and appropriate services.	40	1	5	3.88	0.853
The bank provides sufficient and visible equipments for the customers' use.	40	1	5	3.85	0.736
The bank provides comfortable facilities and designs for customers.	40	1	5	4.05	0.783
Sufficient staffs are available to provide customers banking services.	40	1	5	3.73	0.933
Staffs understand customers' needs.	40	1	5	4.08	0.944
The bank staffs are helpful to customers.	40	1	5	4.08	0.888
<b>Aggregate score</b>				<b>4.06</b>	<b>0.822</b>

Source: Survey Data 2014

The results produced an aggregate mean of 4.06 and SD of .822, an indication of a high rating and moderate distribution diversion. This shows that the banking sector is doing well in the area of bank activities. The factor of banks' provision of customer services as promised was rated thus: above average, 22.5%; good, 37.5%; and excellent, 40%. The results gave a mean of 4.18 and SD of 0.781. The high mean and moderate SD show that the rating was less dispersed. This is due to the

fact that most banks consider customers as the key competitive edge and none of the banks want to lose them to their competitors. The question on bank staff providing personalized services to customers was dispersedly responded to (M=3.90, SD=1.057).

The best rated item on customer service management was security of customers during transaction (M=4.55, SD=.552), where 2.5% was rated above average, 40% as good, and 57.5% as excellent. This means that customers should feel secure at the bank premises during transactions, and, for this, customers become loyal to the banks. With regard to availability of staff to provide banking services to customers, the ratings were: 2.5%, below average; 7.5%, average; 22.5%, above average; 50%, good; and 17.5%, excellent. The results gave a mean of 3.73 and SD of .933. This could be an indication that some banks have sufficient staff, whereas others do not have enough staff.

The entire sector can therefore be considered to be above average on this item. The results were in agreement with earlier studies which linked customer relationship management as a driver of competitive advantage, leading to high performance (Askari, 1991, Yue, 1992, Mavridis, 2004). Also, the results concurred with Zeithmall and Bitner's (1996) recommendation on consideration of the content and delivery of customer service for sustainable market performance. Barnes (1997) argues that the banking industry seems to be the leading service industry on customer service delivery.

Banks value the activities since they are a major driver of competitive advantage. In additional, Alipour (2012) asserts that if the bank fails to handle customer service,

then it fails to achieve its goal. This was supported by secondary data and unstructured interview, which showed that the banks consider their financial performance to be pegged on how they handle customers. Hence the reason why commercial banks aim at treating customers as kings. This has led to introduction of differentiated products to cater for the various customer needs, for instance the Sharia-compliant products (CBK, 2008, 2009, 2010, 2011, 2012, 2013).

#### **4.3.9 Bank Activity Drivers**

To evaluate the role of bank activity driver, the respondents were asked to rate certain factors on a scale of 1-5. The survey data collected was computed and percentages, means and standard deviations presented in Table 4.4.

**Table 4.4 Results of Bank Activity Drivers Rating by Respondents**

Statement	N	Min	Max	Mean	Std. Deviation
The bank's website is easy to use	40	1	5	4.25	0.87
The bank's website is attractive	40	1	5	4.1	1.033
The transactions are secure	40	1	5	4.38	0.838
Bank's website interface accuracy is of required quality	40	1	5	4.2	0.966
Information available is accurate	40	1	5	4.38	0.868
All necessary information is readily available on the site	40	1	5	4.08	1.047
The transactions are error-free	40	1	5	4	1.038
The instructions are clear	40	1	5	4.3	0.823
The information is reliable	40	1	5	4.33	0.829
The telephone banking options are sufficient	40	1	5	3.93	0.917
The waiting time is short	40	1	5	3.8	0.966
The system provides reasonable number of voice prompts	40	1	5	3.7	1.018
Diverse access channels like telephone calls, email, online chat, VOIP calls, etc. are available	40	1	5	4.28	0.847
Call center personnel are knowledgeable to address the various issues	40	1	5	4.15	0.7
Call center contact details are readily available	40	1	5	4.28	0.784
The problem or issue raised is resolved satisfactorily in the first call.	40	1	5	3.88	0.939
The ATMs are conveniently located.	40	1	5	4.08	1.118
The bank provides sufficient number of ATMs.	40	1	5	3.65	1.331
ATMs satisfy all the intended functions	40	1	5	3.8	0.966
Diverse service features are available	40	1	5	4.1	0.871
Wide range of services are available	40	1	5	4.15	0.834
The bank employs the most advanced technology	40	1	5	4.13	0.791
Level of formal education	40	1	5	4.18	0.781
Professional qualifications	40	1	5	4	0.784
Employees' talents	40	1	5	3.9	0.9
Employees' interpersonal skills	40	1	5	4.08	0.797
Employees' knowledge	40	1	5	4.15	0.802
Employees' experience	40	1	5	4.18	0.903
Customer knowledge sharing	40	1	5	3.75	0.84
Employees' knowledge sharing	40	1	5	3.8	0.883
Keeping of company secrets	40	1	5	4.25	1.08
Employees' academic	40	1	5	4.25	0.776
Research work on banking industry	40	1	5	3.25	1.104
Development of new products	40	1	5	3.6	1.057
Innovation of the existing products	40	1	5	3.6	0.955
Employees involvement in decision making	40	1	5	3.5	1.219
Employees' talent development	40	1	5	3.68	1.141
<b>Aggregate score</b>				<b>4.003</b>	<b>0.9302</b>

Source: Survey Data 2014

The results of the survey data gave a mean of 4.00 and SD of .930, indicating that the banking sector is doing quite well on bank activity drivers and this is generally the case across the sector, as evident from the moderate deviation. This could be due to the adoption of new technology which could in turn be due to the youthful management team as seen in demographic data analysis earlier. The data in respect of provision of sufficient number of ATMs resulted in a mean of 3.65 and SD.1.331, showing a moderate rating and a large deviation. Thus, we can conclude that the available number of ATMs is slightly above average, so banks need to increase the number of ATMs. This is necessitated by the fact that most of customers are moving from banking hall services as technology facilitates other banking services via ATM, such as money transfers to other accounts, cash deposits and accessing of bank statements.

Employee academic achievement was rated high, with 20% regarding it as important, 35% viewing it as more important and 45% as very important. The results of the survey gave a mean of 4.25 and SD of 0.776. This indicates that banks value academic achievement and this is in agreement with the earlier analysis of the highest academic level, where majority of the respondents were holders of master's degree. Research work on banking industry was rated poorly, with a mean of 3.25 and SD of 1.104. The percentages were: 5%, not important; 20%, less important; 35%, important; 25%, more important; and 15%, very important.

This is corroborated by Al-Hawari *et al.*, (2005), who cite technology as a key banking activity driver. Shoebridge (2005) states that technology plays an important role in the financial industry. Hence employment of ICT is intensive among the banks. In support of the findings, secondary data and unstructured interview

revealed that technology was considered a key activity driver in the banking industry. Majority of the roles have been automated and human labour is reduced by application of sophisticated electronic machines. This has led to more efficiency and effectiveness in the bank operations as well as aiding in management decisions. Therefore, the study concludes that technology influences the performance of the commercial banks.

The findings were supported by Onyango (2011) who found out that intellectual capital was an important competitive advantage factor among service industries. Kamukama (2011) had a similar view and linked intellectual capital with promotion of a firm's competitive advantage. This is also supported by Wang and Changa (2005) who acknowledged intellectual capital as a fundamental determinant of a firm's current and future competitiveness and value growth. From secondary data and unstructured interview, the study found out that intellectual capital is considered an important component of activity drivers among the commercial banks. However, the commercial banks value knowledge sharing among the staff, so at entry point, banking knowledge is not a priority as banks believe that on-the-job training is more effective than formal trainings. This has led to employment of staff with different professional backgrounds or varied fields so far as formal education is concerned.

#### **4.3.11 Initial Condition**

To assess the role of initial conditions to performance, the respondents were asked to rate initial condition factors on a scale of 1-5, where 1= strongly disagree, 2=disagree, 3=not sure, 4=agree, and 5=strongly agree. Respondents were to indicate the position of their banks in relation to the stated factors by ticking the

corresponding scale. Their responses were computed and percentage, mean and standard deviation presented in Table 4.5.

**Table 4.5 Respondents' Rating of Initial condition**

Statement	N	Min	Max	Mean	Std. Deviation
Firms that began as commercial banks have better performance in the industry.	40	1	5	3.38	1.275
Banks that began as deposit-taking microfinance firms have better opportunity for good performance	40	1	5	3.48	.933
A merger of two banks leads to better performance.	40	1	5	3.35	1.252
Banks that start as branches of the mother bank in another country have a better performance opportunity	40	1	5	3.43	1.035
Banks that start as a franchise of another bank operating in a different country have better chances of good performance	40	1	5	3.23	.974
Banks depend on the vision of the founders for their growth	40	1	5	3.88	.966
The performance of a bank depends on the initial market position	40	1	5	3.25	1.193
Entry strategies influence banks' performance	40	1	5	3.93	.730
<b>Aggregate score</b>				<b>3.488</b>	<b>1.045</b>

Source: Survey Data 2014

The aggregate mean of 3.488 indicates that majority of banks are not sure of the role of initial condition to their firms. The SD of 1.045 is slightly large and shows that banks hold different views in regard to initial condition. The best rated factor is the entry strategies' influence on performance (M=3.93 SD=.730), where 5% disagreed, 15% were not sure, 65.5% agreed and 17.5% strongly agreed. This indicates that banks develop their strategies by modifying the initial strategies of the founders and through innovation. The factor on franchises was poorly rated, with a mean of 3.23 and SD.974, where 2.5% strongly disagreed, 22.5% disagreed, 32.5% were not sure,

35% agreed and only 7.5% strongly agreed. This shows that there is no competitive advantage over the rest for any franchise bank.

From qualitative data analysis, the study found out that most of the respondents did not have important background information of their banks, such as the year when their firm started operating in Kenya. Also, majority of respondents did not know about the initial business of their firm. From the interview, it emerged that most banks concentrate on performance, so their trainings are tailored towards enhancing performance and they rarely discuss their history during staff recruitment and orientation. The dynamism in the sector has led to strategic thinking and planning, focusing on the future instead of the past; hence, many do not consider initial position of the bank to influence its current performance.

This seems to be in agreement with the study by Maina (2011), who found out that location dynamics were considered to influence firm performance more than initial position. Porter (1998) argues that the initial condition is important for firm performance over a period of time, as it determines the market position. However, if one looks at a firm from a specific position without prior knowledge of the initial position, they may fail to acknowledge the effect of the initial conditions.

#### **4.3.12 Managerial Choice**

To examine the effect of managerial choice on performance, respondents were requested to state their bank's view regarding stated factors. They were to rate these managerial choice factors on a scale of 1-5, where 1= strongly disagree, 2= disagree, 3= not sure, 4= agree, and 5 = strongly agree. The collected data was analysed and computed percentages, means and standard deviation presented in Table 4.6.

**Table 4.6 Response Rating on Managerial Choice**

Statement	N	Min	Max	Mean	Std. Deviation
Strategies should be formulated by senior management alone.	40	1	5	2.25	1.171
Not all staff who should be involved in the strategy formulation process.	40	1	5	2.60	1.516
All managers should be allowed to make their own decisions	40	1	5	2.80	1.224
Managers should consolidate their thoughts on major decision-making.	40	1	5	4.15	.864
Not all staff who should be allowed to make their own decisions regarding their roles and duties.	40	1	5	2.70	1.203
Your bank is where it is due to decisions made earlier by managers.	40	1	5	3.35	1.167
<b>Aggregate score</b>				<b>2.975</b>	<b>1.191</b>

Source: Survey Data 2014

An aggregate mean of 2.975 and SD of 1.191 shows a low rating, which can be interpreted to mean that commercial banks' operations support the argument that managerial choices influence bank performance. The argument that strategies should be formulated by senior management alone rated poorly, at  $M=2.25$  and  $SD= 1.171$ , with 30% strongly disagreeing, 37.5 % disagreeing, 15% not sure, 12.5 % agreeing, and 5% strongly agreeing. This means that most banks prefer involvement of other employees in addition to the management in strategy formulation, an indication of the importance of team-work. Majority of the respondents supported the argument that managers should seek the contribution of other employees when making major decisions ( $M=4.15$ ,  $SD= .864$ ), where 7.5% disagreed, 7.5% were not sure, 47.5%

agreed, and 37.5% strongly agreed. This shows that in the banking sector, it is not expected that business be run by an individual's opinion; rather, decisions should involve the input of all staff.

The results were supported by Ayadi and Omolehinwa's (1998) study which found out that poor management contributes to poor bank performance. Thus, managerial choice data ought to be firm-specific, not generalized to a sector. Ghemawat (1991) and Porter (1991) seem to support this finding, as they state that the effect of managerial choice on an organization is only felt after a long period of time. Managerial choices influence performance indirectly and hence may be unrecognized by many people when analyzing performance. However, according to Porter (1998), managerial choices influence firm performance significantly.

#### **4.3.13 Dynamic Capabilities**

To evaluate the role of dynamic capabilities within Kenyan commercial bank sector, the respondents were required to rate stated factors. Respondents were to rate their bank's utilization of sensing dynamic capabilities on a scale of 1-5, where 1= below average, 2= average, 3=above average, 4= good, and 5 = excellent. The computed percentage, mean and standard deviation were presented in Table 4.7.

**Table 4.7 Response Rating on Dynamic Capabilities**

Statement	N	Min	Max	Mean	Std. Deviation
Have ability to direct internal R&D and selecting new technologies.	40	1	5	3.6	1.081
Have ability to tap developments in	40	1	5	3.53	1.062
Have ability to tap supplier and complementor innovation.	40	1	5	3.43	1.035
Have ability to identify target market segments and changing customer needs.	40	1	5	3.83	0.984
Ability to describe the customer solution and the correct business model	40	1	5	3.95	0.876
Ability to select correct decision-making procedures	40	1	5	3.7	0.992
Ability to build loyalty and commitment	40	1	5	4.08	0.764
Ability to select enterprise boundaries to manage complements and "control" platforms	40	1	5	3.85	0.77
Managing strategic fit so that asset combinations are value enhancing.	40	1	5	3.63	0.925
Adopting loosely coupled structures; embracing open innovation; developing integration and Coordination skills.	40	1	5	3.53	0.96
Knowledge management: learning; knowledge transfer; know-how integration; achieving know-how and intellectual property protection.	40	1	5	3.65	0.949
Governance: achieving incentive alignment; minimizing agency issues; Checking strategic malfeasance; Blocking rent dissipation.	40	1	5	3.9	0.982
<b>Aggregate score</b>				<b>3.723</b>	<b>0.948</b>

Source: Survey Data 2014

The computed results indicated a moderate rate with an aggregate mean of 3.723 and SD of 0.948. This can be translated to mean that the banking sector utilization of dynamic capabilities is above average and employees probably need to be enlightened on how to employ these capabilities to achieve better performance. The factor testing the ability of banks to identify target market segments and changing customer needs was rated best, with a mean of 3.83 and SD of 0.984, where 2.5% rated below average, 10% average, 12.5% above average, 52.5% good, and 22.5% excellent. This indicates that commercial banks are alert on market dynamics and customer preferences. The ability to tap suppliers and complementor innovation was rated poorly (M=3.43, SD =1.035), with 2.5% rating below average, 17.5% average,

30% above average, 35% good, and 15% rated excellent. This could indicate a decline in knowledge-sharing outside the bank.

The ability to build loyalty and commitment was rated highest among all the factors, with a mean of 4.08 and SD of 0.764, where 2.5% rated average, 17.5% above average, 50% rated it good, and 30% rated it excellent. This shows that banks employ dynamic capabilities to create and modify loyalty and remain committed to the customers despite the changing environment. Ability to identify the correct decision-making procedure seems to be an area that banks need to employ, seizing DC to improve, which was rated with a mean of 3.70 and SD of 0.992, where 2.5% rated it below average, 10% average, 22.5% above average, 45% good, and only 20% rated it excellent. Governance as a factor was highly rated, with majority, 47.5%, rating it good, 27.5% rated it excellent, 15% above average, 7.5% average, and only 2.5% rated it below average. The mean score was 3.9 and standard deviation was 0.982, indicating that we can generally conclude that banks utilize heavily the transforming DC on governance.

Several scholars support the importance of dynamic capabilities in supporting competitive advantage and performance of firms in dynamic environments (Teece, *et al.*, 1997, Eisenhardt & Martin, 2000, Zahra, *et al.*, 2006). However, Zott (2003) argues that dynamic capabilities are indirectly linked to firm performance, a view that is corroborated by Bowman and Amrosini (2003). Winter (2003) states that DC are essential requirements for any firm to survive in a dynamic environment. From the unstructured interviews, the banks acknowledge the importance of the sensing, seizing and transforming dynamic capabilities in improving their performance in the rapidly changing environment. Secondary data shows that Kenyan banking

environment is quite dynamic and the competition seem to be stiff among the different banks. The study therefore concludes that there is need to understand the employment of DC in the commercial bank sector and assumes that DC influences performance.

#### **4.4 Inferential Statistics Analysis**

To test the hypotheses the researcher conducted simple and multiple regression. However, before carrying out the regression analysis, it was necessary to carry out diagnostic tests as recommended by Field (2009) to confirm the suitability of the data for regression analysis.

##### **4.4.1 Diagnostic Tests**

The following tests were carried out to ensure that the data collected could be analysed via multiple regression. A ratio of cases to independent variable of 5 to 1 is required for multiple regression to be valid, according to Field (2009). The 40 valid cases against 4 independent variables gives a ratio of 10 to 1, thus satisfying the ratio requirement.

##### **a. Tests of Normality**

The study used Shapiro-Wilk to test for the normality of the observed data. The study had 40 observations ( $n=40$ ) and hence Shapiro-Wilk test of normality, which is recommended for  $n < 2000$ , is most appropriate. According to Field (2009), if the test is insignificant ( $p > .05$ ), it implies that the distribution is not significantly different from a normal distribution, hence it is probably normal. However, if the test is significant ( $p < .05$ ), then the distribution in question is significantly different from a

normal distribution, hence it is considered not normal. This test is important because regression model estimation methods are based on the assumption of normality since non-normal data may result in inflated statistics and underestimated standard errors.

**Table 4.8 Shapiro-Wilk Normality Test**

Variable	Shapiro-Wilk	
	Statistic (W)	Sig.
Performance	.968	.301
Initial Condition	.973	.446
Managerial Choices	.954	.106
Activities	.962	.190
Activity Drivers	.971	.389
Dynamic Capabilities	.965	.238

Source: Survey Data 2014

Table 4.8 shows that the p-value for all the variables was more than .05 and hence not statistically significant. Performance had p-value=.301 ( $p > .05$ ); Initial Condition p-value=.446 ( $p > .05$ ); Managerial Choices p-value = .106 ( $p > .05$ ); Activities p-value=.190 ( $p > .05$ ); Activity Drivers P-value =.389 ( $p > .05$ ); and Dynamic Capabilities p-value=.238 ( $p > .05$ ). Hence, the study fails to reject  $H_0$  (the sample data is not different from normal population), implying that the collected data assumed normal distribution for all the variables. Hence, the data could be analyzed via regression as recommended by Hair *et al.*, (2009) and Field (2009).

#### **b. Linearity Test**

The correlation coefficient was used to test the linearity of the relationship between the variables. Correlation coefficient shows the strength as well as the direction of the linear

relationship. Positive correlation indicates a direct influence, where an increase in one variable causes an increase in the other variable, while a negative correlation indicates an inverse relationship, where an increase in one variable caused a decrease in the other (Field, 2009). The weakest linear relationship is indicated by correlation coefficient closeness to 0. The strongest linear correlation is indicated by a correlation of -1 or 1 (Gupta, 2000). The study run Pearson's correlation test and results used to evaluate linear relationship between independent variables and the dependent variable. Table 4.9 shows the results.

**Table 4.9 Pearson's Correlation Coefficients**

		Performance
Banks activities	Pearson Correlation	.636**
	Sig. (2-tailed)	.000
	N	40
Bank activity drivers	Pearson Correlation	.664**
	Sig. (2-tailed)	.000
	N	40
initial conditions	Pearson Correlation	0.226
	Sig. (2-tailed)	0.161
	N	40
managerial choices	Pearson Correlation	.357*
	Sig. (2-tailed)	0.024
	N	40
dynamic capabilities	Pearson Correlation	.591**
	Sig. (2-tailed)	.000
	N	40

\*\* . Correlation is significant at the 0.01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

Source: Survey Data 2014

The results show that all variables had linear relationship with performance, according to Gupta (2000) and Field (2009). However, the relationship was weakest between performance and initial condition ( $r = 0.226$ ,  $p = .161$ ). The relationship was

strongest between performance and activity drivers ( $r = .664$ ,  $p = .000$ ) as well as performance and bank activities ( $r = .636$ ,  $p = .000$ ). Relationships between performance and dynamic capabilities ( $r = .591$ ,  $p = .000$ ) as well as performance and managerial choice ( $r = .357$ ,  $p = .024$ ) were also strong. Hence, for the study, the assumption of linearity for regression test was achieved.

### c. Multi-collinearity Test

Multi-collinearity is a problem that exists when two or more independent variables are highly correlated with each other. This may have a negative effect on regression models and thus a proper multi-collinearity diagnostic test should be conducted to avoid misleading results. Field (2009) recommends the use of tolerance values and variance inflated factor (VIF) values to carry out this diagnosis. A tolerance value less than 0.2 indicates serious collinearity problem. A VIF value of above 5 indicates presence of multi-collinearity, and a mean VIF above 2 should be of concern (Hair *et al.*, 2010). Multi-collinearity test was run and Table 4.10 presents the tolerance and VIF values for the variables under study.

**Table 4.10 Multi-collinearity Test**

	Collinearity Statistics	
	Tolerance	VIF
Banks Activities	.427	2.343
Bank Activity Drivers	.405	2.470
Initial Conditions	.745	1.342
Managerial Choices	.965	1.036
Dynamic Capabilities	.503	1.988
Mean	<b>.635</b>	<b>1.798</b>

Dependent Variable: Performance

Source: Survey Data 2014

The results show that all the variables have a VIF of less than 5 and tolerance value of more than 0.2. The mean VIF is 1.798 (below 10), so the study rules out the possibility of multi-collinearity. Hence, the data regression analysis could be carried out to explain the relationship between the independent variables and dependent variables.

#### **4.5 Hypotheses Testing**

After the successful running of the preliminary diagnostic tests and confirming that the data complied with the prerequisite assumptions, regression analyses were performed on the data to test the hypotheses.

##### **4.5.1 Testing Hypothesis One**

*H<sub>01</sub>. There is no relationship between bank activities and performance of commercial banks in Kenya.*

To analyse the relationship between banks' activities and performance, the study used Hypothesis One. The following model was used and a linear regression was run to test the Hypothesis One.

$$BP = \alpha + \beta BA + \varepsilon \dots \dots \dots (i)$$

The relevant regression results for the model are presented in Tables 4.11

**Table 4.11 Regression Results for Bank Activities on Performance**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate		
1	.636 <sup>a</sup>	.405	.389	.46977		
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.700	1	5.700	25.829	.000 <sup>b</sup>
	Residual	8.386	38	.221		
	Total	14.086	39			
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.935	.572		1.634	.111
	Banks Activities	.742	.146	.636	5.082	.000

a. Dependent Variable: Performance

b. Predictors: (Constant), Banks Activities

Source Survey Data 2014

The summary model shows a positive moderate linear relationship between bank activities and performance ( $r=.636$ ). Adjusted  $R^2$  of .389 means that 38.9% variance in commercial bank performance can be attributed to bank activities, while the remaining could be attributed to other factors not included in the model.

The overall model was statistically significant ( $F_{(1, 38)} = 25.829$ ,  $p\text{-value} = .000$ ). Based on the regression results, the null hypothesis was rejected and the study concluded that bank activities have a significant effect on Kenyan commercial bank sector. The results are in agreement with Heffernan, *et al.*, (2008) study which indicated that there is a significant correlation between customer-related activities and performance. Also, the study supported the findings of work by Woodruff (1997) and Payne, *et al.*, (2008) that firm activities are key drivers of competitive advantage and positively influence performance significantly. The regression

equation of bank activities and performance can be summarized as follows:

$$\text{Performance} = 0.935 + 0.742 * \text{banks activities} + \epsilon$$

**4.5.2 Testing Hypothesis Two**

*H<sub>02</sub>. There is no relationship between bank activity drivers and performance of commercial banks in Kenya.*

Hypothesis Two was used to investigate the relationship between bank activity drivers and performance of commercial banks in Kenya. Equation Two was used to explain the effect of bank activity drivers on performance and was stated as follows.

$$BP = \alpha + \beta BAD + \epsilon \dots\dots\dots(ii)$$

This was regressed on performance and the relevant results were presented in Tables 4.12.

**Table 4.12 Regression Results for Bank Activity Drivers on Performance**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate		
1	.664 <sup>a</sup>	.440	.426	.45549		
Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	6.202	1	6.202	29.894	.000 <sup>b</sup>
1	Residual	7.884	38	.207		
	Total	14.086	39			
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
	(Constant)	.861	.546		1.577	.123
1	Bank Activity Drivers	.739	.135	.664	5.468	.000

- a. Dependent Variable: Performance
- b. Predictors: (Constant), Bank Activity Drivers

Source Survey Data 2014

The regression results indicate strong relationship between activity drivers and performance at  $r=.664$ . The model adjusted  $R^2$  of .426 implies that 42.6% of variance in bank performance can be explained by bank activity drivers, while the remainder can be explained by other variables not considered in the model.

The results indicate the fitness of the regression model  $F_{(1, 38)} = 29.894$  and p-value  $=.000$  ( $p<.05$ ), thus the model is statistically significant, supporting rejection of null hypothesis. Hence, we can conclude that bank activity drivers have a significant effect on performance of commercial banks in Kenya.

The model regression coefficients presented in Table 4.12 help in summarizing the regression model as follows:

$$\text{Performance} = 0.861 + 0.739 * \text{Bank Activity Drivers} + \epsilon.$$

The results were in agreement with Liebach and Flohr (2003) who found that activity drivers lead to the bank's high performance. Acharya, *et al.*, (2008) suggested that the application of activity drivers lead to improvement of bank performance. Other studies that have linked bank activity drivers with significant effect on performance include the ones of Chen, *et al.*, (2005), Mwanja and Muganda (2010), Zou and Huan (2011), and Aliyu and Tasmin (2012). The study concludes that bank activity drivers have significant effect on performance in Kenyan commercial bank sector.

#### 4.5.3 Testing Hypothesis Three

*H<sub>03</sub>. There is no relationship between Initial Conditions and performance of commercial banks in Kenya.*

Hypothesis Three was used to determine the relationship between Initial Conditions and performance of Kenyan commercial banks. Equation Three was used for the Regression Model on effect of initial condition on performance.

$$BP = \alpha + \beta IC + \varepsilon \dots \dots \dots (iii)$$

Initial Conditions was regressed on Performance and the results presented in Table 4.13

**Table 4.13 Regression Results for Initial Conditions on Performance**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate		
1	.226 <sup>a</sup>	.051	.026	.59306		
Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	.720	1	.720	2.048	.161 <sup>b</sup>
1	Residual	13.365	38	.352		
	Total	14.086	39			
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.821	.704		4.006	.000
	Initial Conditions	.291	.203	.226	1.431	.161

a. Dependent Variable: Performance

b. Predictors: (Constant), Initial Conditions

Source Survey Data 2014

Table 4.13 shows a weak relationship between Initial Conditions and Performance at  $r = .226$ . The model adjusted  $R^2$  of .026 implies that only 2.6% of variance in bank performance can be explained by Initial Conditions, while the remainder can be explained by other variables not considered in the model.

The fitness of the regression model  $F_{(1, 38)} = 2.048$  and p-value = .161 ( $p > .05$ ), thus the model is statistically not significant. This implies that we should fail to reject the null hypothesis and conclude that there is no relationship between Initial Conditions and Performance of commercial banks in Kenya.

This finding seems to go against the expectation of majority of scholars. However, empirical review indicated that the market dynamism of Kenya commercial bank sector has provoked strategic thinking and planning. Therefore, banks tend to focus on the future other than the past. This was in agreement with Maina (2011) who found out that location dynamics were considered to influence firm performance more than initial position. Porter (1998) argues that Initial Conditions is important for firm performance over a period of time, as it determines the market position. However, looking at a firm from a specific position without prior knowledge of the initial position may lead to failure of acknowledging the effect of the Initial Conditions.

The findings were also supported by Hsiu-Ling, Chen and Shiu (2007) whose study found that the impact of Initial Conditions on Performance diminishes with age. This could have been the case since most of commercial banks in Kenya have been in operation for more than 20 years. Tan and Floros (2012) suggest that Initial Conditions has less effect on Performance in a dynamic market environment.

#### **4.5.4 Testing Hypothesis Four**

*H<sub>04</sub>. There is no relationship between managerial choice and performance of commercial banks in Kenya*

To determine the relationship between managerial choices and performance of commercial banks in Kenya, Hypothesis Four was applied. Equation Four was used for the Regression Model to show the effect of managerial choices on Performance.

$$BP = \alpha + \beta MC + \varepsilon \dots \dots \dots (iv)$$

Managerial Choice was regressed on Performance and the results were presented in Table 4.14

**Table 4.14 Regression Results for Managerial Choice on Performance**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate		
1	.357 <sup>a</sup>	.127	.104	.56875		
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.794	1	1.794	5.545	.024 <sup>b</sup>
	Residual	12.292	38	.323		
	Total	14.086	39			
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.174	.705		3.085	.004
	Managerial Choices	.464	.197	.357	2.355	.024

a. Dependent Variable: Performance

b. Predictors: (Constant), Managerial Choices

Source Survey Data 2014

The regression results indicates moderate relationship between Managerial Choice and Performance at  $r=.357$ . The model adjusted  $R^2$  of .104 implies that 10.4% of variance in bank performance can be explained by managerial choice, while the remainder can be explained by other variables not considered in the model.

The results indicate the fitness of the Regression Model  $F_{(1, 38)} = 5.545$  and p-value  $=.024$  ( $p<.05$ ), thus the model is statistically significant, supporting rejection of  $H_0$ . Hence, we can conclude that Managerial Choice have a significant effect on Performance of commercial banks in Kenya.

The model regression coefficients help in summarizing the Regression Model as follows: Performance =  $2.174 + 0.464 * \text{Managerial Choice} + \epsilon$ .

Zollo and Winter (2002) point out that managerial choices determine the routines and capabilities to be employed in a firm and indirectly influence performance in dynamic environment. Schreyögg and Kliesch-Eberl (2007) proposed the consideration of capability monitoring as an important role of management based on the choices that they may make, since it influences the performance of the firm. To enables a firm diffuse market information effectively across all relevant functional areas that can be exploited to direct new product development processes, then the correct managerial choices ought to be made (Nielsen, 2006; Helfat *et al.*, 2007).

Porter (1991) observes that pure managerial choices lead to the assembly or creation of the particular skills and resources required to carry out new strategies. The skills and market position possessed by any firm today are viewed as the result of past managerial choices about how to configure activities and skills creation or acquisition. According to Ghemawat (1991), some of these choices involve hard-to-reverse commitments or path dependency. Once managers understand their competitive environment and source of their competitive advantages, then they are able to creatively search for favourable positions, assemble the needed skills and assets, configure the value chain appropriately, and put in place supportive organizational routines and culture that reinforces the required internal behavior. All these are determined by the choices the managers make but have a direct influence on the firm performance (Ghemawat, 1991; Porter, 1991).

#### **4.5.5 Testing Hypothesis Five**

*H<sub>05</sub>. There is no relationship between joint effect of drivers of competitive advantage and performance of commercial banks in Kenya.*

To determine the relationship between the joint effect of drivers of competitive advantage and performance of commercial banks in Kenya, Hypothesis Five was applied. Equation Five was used for the Regression Model to show the effect of drivers of competitive advantage on performance.

$$BP = \alpha + \beta BA + \beta BAD + \beta IC + \beta MC + \varepsilon \dots \dots \dots (v)$$

Bank Activities, Bank Activity Drivers, Initial Conditions and Managerial Choice were regressed on performance and the results were presented in Table 4.15

**Table 4.15 Regression Results for Drivers of Competitive Advantage on Performance**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate		
1	.746 <sup>a</sup>	.557	.507	.42212		
Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	7.849	4	1.962	11.012	.000 <sup>b</sup>
1	Residual	6.237	35	.178		
	Total	14.086	39			
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
	(Constant)	-.199	.755		-.264	.794
	Banks Activities	.391	.190	.335	2.056	.047
1	Bank Activity Drivers	.480	.190	.431	2.532	.016
	Initial Conditions	-.149	.163	-.116	-.913	.368
	Managerial Choices	.307	.149	.236	2.062	.047

a. Dependent Variable: Performance

b. Predictors: (Constant), Managerial Choices, Initial Conditions, Banks Activities, Bank Activity Drivers

Source Survey Data 2014

The overall model was statistically significant ( $F_{(4, 35)} = 11.012$ ,  $p\text{-value} = .000$ ). The adjusted  $R^2$  of 0.507 indicated that 50.7% of the variance in commercial banking sector's performance can be attributed to the model, while the remaining percentage could be explained by other factors not included in this study. R squared of .557

indicated that the study variables could explain 55.7% performance variance of commercial banks sector in Kenya.

The beta coefficient for the banks' activities was 0.391 with a p-value 0.047 (<.05). This indicates that a statistically significant relationship between banks' activities and their performance. Based on these findings, the null hypothesis was rejected. Therefore, the study assumed that bank activities have a significant effect on the Kenyan commercial bank sector. The beta coefficient for bank activity drivers was 0.480, p-value 0.016 (<.05). This supported rejection of H<sub>02</sub>. The beta coefficient for initial conditions -0.149, p-value 0.368 (>0.05) supported not rejecting H<sub>03</sub>, while the beta coefficient for managerial choice 0.307, p-value of 0.047 (< 0.05) supported rejection of H<sub>04</sub>.

The Regression Model was summarized as follows:

$$\text{Performance} = 0.391 * \text{Bank Activities} + 0.48 * \text{Bank Activity Drivers} + 0.307 * \text{Managerial Choice} - 0.149 * \text{Initial Conditions} - 0.199 + \epsilon.$$

The overall model has a p-value 0.000 (<.05), supporting rejection of H<sub>05</sub>. Hence, the study concludes that there is significant relationship between drivers of competitive advantage and performance of commercial banks in Kenya.

#### 4.5.6 Testing Hypothesis Six

*H<sub>06</sub>. Dynamic capabilities do not have moderating effect on the relationship between drivers of Competitive Advantage and performance of commercial banks in Kenya.*

Hypothesis Six was used to test the moderating effect of dynamic capabilities on the relationship between drivers of competitive advantage and performance of

commercial banks in Kenya. To test this hypothesis, Hierarchical Multiple Regressions was applied. Equation Six was used for the Regression Model to show the moderating effect of Dynamic Capabilities on the relationship between drivers of competitive advantage and performance.

**Table 4.16 Regression Results for Moderating Effect of Dynamic Capabilities**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F	df1	df2	Sig. F Change
1	.746 <sup>a</sup>	.557	.507	.42212	.557	11.012	4	35	.000
2	.769 <sup>b</sup>	.591	.531	.41176	.034	2.784	1	34	.104

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	7.849	4	1.962	11.012	.000 <sup>b</sup>
	Residual	6.237	35	.178		
	Total	14.086	39			
2	Regression	8.321	5	1.664	9.816	.000 <sup>c</sup>
	Residual	5.765	34	.170		
	Total	14.086	39			

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.199	.755		-.264	.794
	Banks activities	.391	.190	.335	2.056	.047
	Bank activity drivers	.480	.190	.431	2.532	.016
	initial conditions	-.149	.163	-.116	-.913	.368
	managerial choices	.307	.149	.236	2.062	.047
2	(Constant)	-.076	.741		-.103	.919
	Banks activities	.286	.196	.245	1.459	.154
	Bank activity drivers	.394	.192	.354	2.051	.048
	initial conditions	-.211	.164	-.164	-1.289	.206
	managerial choices	.309	.145	.237	2.126	.041
	dynamic capabilities	.227	.136	.258	1.669	.104

a. Predictors: (Constant), Managerial Choices, Initial Conditions, Bank Activities, Bank Activity Drivers

b. Predictors: (Constant), Managerial Choices, Initial Conditions, Bank Activities, Bank Activity Drivers, Dynamic Capabilities

Source Survey Data 2014

The results show a change of  $R^2$  by .034, which means that the Moderated Model increased by 3.4%. Adjusted  $R^2$  changed from 0.507 to 0.531, indicating a 2.4% improvement of variance of performance, explained by the Moderated Model.

The results indicate that the two models were statistically significant. Model 1 had  $F_{(4, 35)} = 11.012$  and  $p\text{-value} = .000$  ( $p < .05$ ), while model 2 had  $F_{(5, 34)} = 9.816$  and  $p\text{-values} = .000$  ( $p < .05$ ) hence support the rejection of  $H_06$ . Beta coefficients of Bank Activity Drivers  $p\text{-value} = .048$  and Managerial Choice  $p\text{-value} = .041$  were significant at  $p < .05$  in the Moderated Model. The moderating variable (dynamic capabilities),  $p\text{-value} = .104$ , was not significant at  $p < .05$ .

Based on the moderation rule by MacKinnon, Fairchild, & Fritz, (2007), Dynamic Capabilities has a moderating effect on the relationship between drivers of Competitive Advantage and Performance of commercial banks in Kenya. Hence, we reject the null hypothesis and conclude that Dynamic Capabilities have moderating effect on the relationship between drivers of Competitive Advantage and Performance of commercial banks in Kenya. The findings support that Dynamic Capabilities influences the relationship between the drivers of Competitive Advantage and Performance among the commercial banks in Kenya directly and indirectly.

The findings were in agreement with the findings of the study by Zott (2003), linking DC indirectly to Performance and stating their influence on drivers of Competitive Advantage. Bowman and Ambrosini (2003), support the indirect effect of DC on Performance, whereas Helfat *et al.*, (2007) argue that DC do not lead to competitive advantage but influence drivers of CA.

**Table 4.17 Summary of Hypotheses Testing**

	Null Hypothesis	Result
H <sub>O1</sub>	There is no relationship between bank activities and performance of commercial bank in Kenya.	Hypothesis was rejected
H <sub>O2</sub>	There is no relationship between bank activity drivers and performance of commercial bank in Kenya.	Hypothesis was rejected
H <sub>O3</sub>	There is no relationship between initial conditions and performance of commercial banks in Kenya.	Hypothesis was not rejected
H <sub>O4</sub>	There is no relationship between managerial choice and performance of commercial banks in Kenya.	Hypothesis was rejected
H <sub>O5</sub>	There is no relationship between drivers of competitive advantage and performance of commercial banks in Kenya.	Hypothesis was rejected
H <sub>O6</sub>	Dynamic capabilities do not have any moderating effect on the relationship between drivers of competitive advantage and performance of commercial banks in Kenya.	Hypothesis was rejected

Source: survey data 2014

## **CHAPTER FIVE**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Introduction**

This chapter presents the summary of the study, conclusions, and contributions of the study to knowledge, recommendations on areas that need further research.

#### **5.2 Summary**

The market of the Kenyan commercial banks sector has been changing rapidly, while the sector faces stiff competition. Despite this, the commercial bank sector performance is better than that of many other sectors. However, some banks within the sector have poorer performance than others as shown by financial performance indicators. This calls for investigation on the drivers of competitive advantage influencing performance in the sector. There was also a need to evaluate the moderating role of dynamic capabilities in the relationship between drivers of competitive advantage and performance of commercial banks in Kenya due to the rapid changes facing the sector's market.

The study was guided by six specific objectives as follows: To evaluate the influence of bank activities on performance of commercial banks in Kenya; to assess the influence of bank activity drivers on performance of commercial banks in Kenya; to determine the influence of initial condition on performance of commercial banks in Kenya; to determine the influence of managerial choice on performance of commercial banks in Kenya; to determine the influence of drivers of competitive

advantage on performance of commercial banks sector in Kenya; and to determine the moderating effect of dynamic capabilities on the relationship between drivers of competitive advantage and performance of commercial banks in Kenya.

To achieve this, the study used exploratory research design. A census of all the 43 commercial banks was carried out. Data was collected using semi-structured questionnaire and secondary data gathering tool. The collected data was analysed using descriptive and inferential statistics.

The results indicated that banking activities positively influence commercial bank performance in Kenya. Also, the results showed that bank activity drivers had positive and statistically significant influence on the performance of commercial banks in Kenya. The relationship between managerial choices and performance was positive and statistically significant. The result on the relationship between initial conditions and performance was weak, positive but statistically insignificant. This was explained by empirical studies that the relationship between initial conditions and performance become weaker with time and, notably, many commercial banks have been operating in the Kenyan market for more than 20 years. The study found dynamic capabilities to positively influence the relationship between drivers of competitive advantage and performance as a moderator.

## **5.2 Conclusion**

The results indicated a positive significant relationship between the drivers of competitive advantage, initial conditions and performance of the commercial banks sector in Kenya. The study concludes that bank activities significantly influence the performance of commercial banks. Also, the results showed that bank activity

drivers have a significant influence on performance of Kenyan commercial banks. This study found the relationship between initial conditions and performance as statistically insignificant. This leads to the conclusion that initial conditions do not significantly influence commercial bank performance in Kenya. The study also found the relationship between managerial choices and performance to be positive and significant. Hence, the study concludes that managerial choices significantly influence performance of banks in Kenya. The results indicated that dynamic capabilities have a moderating role between the drivers of competitive advantage and performance of commercial banks in Kenya. The moderating effect was positive and statistically significant.

### **5.3 Recommendations and Policy Implications**

The findings of this study can be used to draw various conclusions on the performance of the commercial bank sector in Kenya and the recommendations made may only be limited to this sector. Bank activities were found to be positively significant, influencing performance; hence, managers should enhance training to improve the skills of their staff on customer service delivery and management of customer relationship. The firms should empower their research and design departments to facilitate the understanding of customer preference changes of products and services. Customer service department should constitute highly trained personnel with proper knowledge of the customers' current needs and available products so as to respond to customer queries on first meeting. The Kenya government through the Ministry of Finance and in collaboration with CBK and KBA should develop policies on the qualification of customer service officers in the

commercial banks and monitor the way they work to ensure world class services are offered to all customers.

The results indicated significant positive influence of bank activity drivers on performance of commercial bank sector in Kenya, implying their importance. The commercial bank managements should therefore ensure employment of cutting-edge technology to support their banks' performance. The KBA should lobby for application of the most recent technology by its members for use by the R&D department in conjunction with the ICT department for capacity building and training. CBK should also lobby for the application of the right technology and monitor technological infrastructure in all commercial banks. KBA and CBK should also ensure that all bank employees are highly skilled and willing to keep retrainig so as to keep up with the industry's dynamism. The banks should also have robust training programs with a view to uplifting their intellectual capital.

The results indicated positive significant influence of managerial choices on performance of commercial banking sector in Kenya, implying their importance. Therefore, the owners of the banks should ensure the employment of the right management personnel and also give the managers room for decision-making on behalf of the bank. KBA and CBK should stipulate the minimum qualifications that top management staff should have. The aim of this should be to ensure that the right people hold key positions so as to maintain and, better still, improve the bank performance and improved performance of the whole sector. KBA and CBK should lobby for the development of integrity and attitude tests for all bank management to ensure that bank decisions are made by the right people.

Since the results showed that dynamic capabilities play a moderation role on the relationship between drivers of competitive advantage and performance, the study recommends that the management should lobby for training of all employees so as to understand the application of dynamic capabilities within their firms. They should ensure that all staff are trained to appreciate the volatility of their market and how to respond to change in an effort to address any new challenges. The management should lobby to have the government provide level playing ground in all industries so as to allow the firms utilize DCs for their CA gain. KBA and CBK should also lobby for intensive training on DCs within the banking industry.

#### **5.4 Recommendation for Further Research**

Based on the research findings of this study, further studies should be conducted to enrich the body of knowledge in the area of performance in a dynamic environment. There should also be similar studies carried out using the longitudinal survey method. Also, similar study should be carried out in to validate the findings of this research. The researcher also recommends further studies that take into account other drivers of competitive advantage, not included in this study.

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## APPENDICES

### **Appendix A: Introduction Letter**

My name is Julius Kahuthia Mwangi and I am pursuing PhD in strategic management at Kenyatta University. As a requirement for the program, I am carrying out a research on “**Drivers of Competitive Advantage and Performance of Commercial Banks in Kenya**”. In this connection, I am gathering certain information from all commercial banks, from one representative per bank, and you have been selected to furnish me with the information that I require by your bank. I will greatly appreciate your assistance.

This questionnaire is for academic research purposes only and I undertake to maintain the highest level of confidentiality so far as the participants are concerned. Please do not write your name, contact or the name of your firm anywhere within this questionnaire.

There are two parts of the questionnaire: Part One concerns personal information, while Part Two is about the research questions. Kindly spare about 15 minutes and answer the questions in the questionnaire truthfully.

Thanks in advance for accepting to take part in this research.

Yours sincerely,

Julius Kahuthia Mwangi

Tel 0720 538 669

Email:kahuthiamwangi@yahoo.com

**Appendix B: Questionnaire**

**PART ONE**

**A. Bank's information**

Which year did your bank start operating in Kenya?.....

What was the original activity of your bank? .....

Has your bank changed from the original operation? Yes/ NO

If yes, why did the bank change from the original activity?.....

How many branches did your bank have at the beginning? .....

How many branches does your bank have, currently? .....

Approximately how many employees did the bank have at the beginning? .....

Approximately how many employees does the bank have currently? .....

Approximately how many managers did the bank have at the beginning? .....

Approximately how many managers does the bank have, currently? .....

## PART TWO

### Question 1

#### Performance

Kindly use the scale of 1-5 (1= below average; 2= average; 3= above average; 4= good; 5= excellent) to answer the question.

How does your organization rate in the following, compared to other commercial banks?

a	Overall performance	1	2	3	4	5
b	Profit before tax	1	2	3	4	5
c	Profit after tax	1	2	3	4	5
d	Return on investment	1	2	3	4	5
e	Return on assets	1	2	3	4	5
f	Return on equity	1	2	3	4	5
g	Customer base growth	1	2	3	4	5
h	Development of new products	1	2	3	4	5
i	Adoption and application of new technology	1	2	3	4	5
j	Innovation	1	2	3	4	5
k	Staff retention within the bank	1	2	3	4	5
l	Opening of new branches	1	2	3	4	5
m	New ATM machines and sites	1	2	3	4	5

### Question 2

#### Customer service delivery

Please use the scale of 1 – 5 (1 = below average, 2 = average, 3 = above average, 4 = good, 5 = excellent) to answer the question.

To what extent do the following describe your bank in comparison with entire commercial bank sector?

a	The bank provides customers services as promised	1	2	3	4	5
b	The bank provides accurate service to customers	1	2	3	4	5
c	The bank honors its commitments.	1	2	3	4	5
d	Bank staffs know how to solve customers' problems.	1	2	3	4	5
e	Staffs have the enthusiasm to understand customer needs.	1	2	3	4	5

f	Staffs consider customer needs first.	1	2	3	4	5
g	Staff can provide customers with precise personal services	1	2	3	4	5

### Question 3

#### Customer Relationship Management

Please use the scale of 1 – 5 (1 = below average, 2 = average, 3 = above average, 4 = good, 5 = excellent) to answer the question.

How does your bank rate in the following compared to other banks in the commercial bank sector?

a	The bank ensures security of customers during the transaction process	1	2	3	4	5
b	The bank provides quality services, thus increasing customers' confident and trust.	1	2	3	4	5
c	Bank staffs provide customers prompt and appropriate services.	1	2	3	4	5
d	The bank provides sufficient and visible equipments for customers' usage.	1	2	3	4	5
e	The bank provides comfortable facilities and of good design to customers.	1	2	3	4	5
f	Sufficient staffs are available to provide customers with banking services.	1	2	3	4	5
g	Staffs understand customers' needs.	1	2	3	4	5
h	The bank has helpful staff for customers.	1	2	3	4	5

### Question 4

#### Technology

Please use the scale of 1 – 5 (1 = below average, 2 = average, 3 = above average, 4 = good, 5 = excellent) to answer the question.

How does your bank rate in the following?

#### 1 *Internet Banking*

a	The bank's website is easy to use	1	2	3	4	5
b	The bank's website is attractive	1	2	3	4	5
c	The transactions are secure	1	2	3	4	5
d	The bank's website interface accuracy is of required quality	1	2	3	4	5
e	Information available is accurate	1	2	3	4	5
f	All necessary information is readily available on the site	1	2	3	4	5

g	The transactions are error free	1	2	3	4	5
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## 2 Telephone Banking Services

a	The instructions are clear	1	2	3	4	5
b	The information is reliable	1	2	3	4	5
c	The telephone banking options are sufficient	1	2	3	4	5
d	The waiting time is short	1	2	3	4	5
e	The system provides a reasonable number of voice prompts	1	2	3	4	5

## 3 Call Center Services

a	Diverse access channels like telephone calls, email, online chat, VOIP calls, etc. are available	1	2	3	4	5
b	Call center personnel are knowledgeable enough to address the various issues	1	2	3	4	5
c	Call center contact details are readily available	1	2	3	4	5
d	The problem or issue raised is resolved satisfactorily in the first call	1	2	3	4	5

## 4 ATM Services

a	The ATMs are conveniently located	1	2	3	4	5
b	The bank provides sufficient number of ATMs	1	2	3	4	5
c	ATMs satisfy all the intended functions	1	2	3	4	5

## 5 Core Service

a	Diverse service features are available	1	2	3	4	5
b	Wide range of services are available	1	2	3	4	5
c	The bank employs the most advanced technology	1	2	3	4	5

### Question 5

#### Intellectual Capital

Please use the scale of 1 – 5 (1 = not important, 2 = less important, 3 = important, 4 = more important, 5 = very important) to answer the question.

How important are the following during recruiting, promoting or transferring of staff within your bank?

A	Level of formal education	1	2	3	4	5
B	Professional qualifications	1	2	3	4	5

C	Employees' talents	1	2	3	4	5
D	Employees' interpersonal skills	1	2	3	4	5
E	Employees' knowledge	1	2	3	4	5
F	Employees' experience	1	2	3	4	5
G	Customer knowledge sharing	1	2	3	4	5
H	Employees' knowledge sharing	1	2	3	4	5
I	Keeping company secrets	1	2	3	4	5
J	Employees' academic qualifications	1	2	3	4	5
K	Research work on banking industry	1	2	3	4	5
L	Development of new products	1	2	3	4	5
M	Innovation of the existing products	1	2	3	4	5
N	Employees' involvement in decision making	1	2	3	4	5
O	Employees' talent development	1	2	3	4	5

### Question 6

#### Initial condition

Please use the scale of 1 – 5 (1 = strongly disagree, 2 = disagree, 3 =not sure, 4 = agree, 5 = strongly agree) to answer the question.

On the following statements, what are you bank's view?

A	Firms that began as commercial banks have better performance in the commercial bank sector.	1	2	3	4	5
B	Banks that began as deposit-taking microfinance firms have better opportunity of performing in the commercial bank sector.	1	2	3	4	5
C	A merger of two banks leads to better performance.	1	2	3	4	5
D	Banks that start as branches of other banks in other countries have better performance opportunity	1	2	3	4	5
E	Banks that start as franchises of other banks operating in different countries have better chances of performing	1	2	3	4	5
F	Banks depend on the vision of the founders for their growth	1	2	3	4	5
G	The performance of a bank depends on the initial market position	1	2	3	4	5
H	Entry strategies influence banks performance	1	2	3	4	5

**Question 7****Managerial choice**

Please use the scale of 1 – 5 (1 = strongly disagree, 2 = disagree, 3 =not sure, 4 = agree, 5 = strongly agree) to answer the question.

What is your organization's position in regard to the following?

A	Strategies should be formulated by senior management alone.	1	2	3	4	5
B	Not all staff who should be involved in the strategy formulation process.	1	2	3	4	5
C	Not all managers should be allowed to make their own decision	1	2	3	4	5
D	Managers should consolidate their thoughts on major decision-making.	1	2	3	4	5
E	Not all the staff should be allowed to make their own decisions regarding their roles and duties.	1	2	3	4	5
F	Your bank is where it is due to decisions made earlier by managers.	1	2	3	4	5
G	Every decision made by managers has an impact on the bank performance.	1	2	3	4	5

**Question 8****Sensing dynamic capabilities**

Please use the scale of 1 – 5 (1 = below average, 2 = average, 3 = above average, 4 = good, 5 = excellent) to answer the question.

How does your bank rate in comparison with the best performer in the sector in respect of the following?

a	Has the ability to direct internal R&D and in selecting new technologies.	1	2	3	4	5
b	Has the ability to tap developments in general science and technology.	1	2	3	4	5
c	Has the ability to tap Supplier and Complementor Innovation.	1	2	3	4	5
d	Has the ability to identify target market segments and changing customer needs.	1	2	3	4	5

**Question 9****Seizing dynamic capabilities**

Please use the scale of 1 – 5 (1 = below average, 2 = average, 3 = above average, 4 = good, 5 = excellent) to answer the question.

How does your bank rate in the following in comparison with the best performer in the sector?

a	Ability to describe the customer solution and the correct business model	1	2	3	4	5
b	Ability to select correct decision-making procedures	1	2	3	4	5
c	Ability to build loyalty and commitment	1	2	3	4	5
d	Ability to select enterprise boundaries to manage complements and “control” platforms.	1	2	3	4	5

**Question 10****Transforming dynamic capabilities**

Please use the scale of 1 – 5 (1 = below average, 2 = average, 3 = above average, 4 = good, 5 = excellent) to answer the question.

How does your bank perform the following in comparison to the best performer in the sector?

a	Managing strategic fit so that asset combinations are value-enhancing.	1	2	3	4	5
b	Adopting loosely coupled structures; embracing open innovation; developing integration and coordination skills.	1	2	3	4	5
c	Knowledge Management: learning; knowledge transfer; know-how integration; achieving know-how and intellectual property protection.	1	2	3	4	5
d	Governance: achieving incentive alignment; minimizing agency issues; checking strategic malfeasance; blocking rent dissipation.	1	2	3	4	5

**Thank you very much for taking part in this exercise.**

**May God bless you abundantly.**

**Appendix C: Secondary Data Collection Tool.**

**Section 1: Non Financial Data**

Bank name	Peer Group					Customer Base Increase (%)				
	2009	2010	2011	2012	2013	2009	2010	2011	2012	2013

Source: Researcher 2014

**Section 2: Financial Data**

Bank name	Profit before Tax Increase (%)					ROA					ROE				
	2009	2010	2011	2012	2013	2009	2010	2011	2012	2013	2009	2010	2011	2012	2013

Source: Researcher 2014

## Appendix D: Summary of Commercial Banks Peer Grouping

**Table D: Summary of Peer Grouping, based on Market Share**

Bank name	Peer Grouping					
	2008	2009	2010	2011	2012	2013
Barclays Bank of Kenya	Large	Large	Large	Large	Large	Large
CFC Stanbic Bank	Large	Large	Large	Large	Large	Large
Co-operative Bank of Kenya	Large	Large	Large	Large	Large	Large
Equity Bank	Large	Large	Large	Large	Large	Large
Kenya Commercial Bank	Large	Large	Large	Large	Large	Large
Standard Chartered Bank Kenya	Large	Large	Large	Large	Large	Large
Bank of Africa Kenya	Medium	Medium	Medium	Medium	Medium	Medium
Bank of Baroda (Kenya)	Medium	Medium	Medium	Medium	Medium	Medium
Bank of India	Medium	Medium	Medium	Medium	Medium	Medium
Chase Bank (Kenya)	Medium	Medium	Medium	Medium	Medium	Medium
Citibank N.A. Kenya	Medium	Medium	Medium	Medium	Medium	Medium
Commercial Bank of Africa Ltd	Medium	Medium	Medium	Medium	Medium	Medium
Diamond Trust Bank Kenya	Medium	Medium	Medium	Medium	Medium	Medium
Ecobank Kenya	Medium	Medium	Medium	Medium	Medium	Small
Family Bank	Medium	Medium	Medium	Medium	Medium	Medium
I & M Bank	Medium	Medium	Medium	Medium	Medium	Medium
Imperial Bank	Medium	Medium	Medium	Medium	Medium	Medium
National Bank of Kenya	Medium	Medium	Medium	Medium	Medium	Medium
NIC Bank	Medium	Medium	Medium	Medium	Medium	Medium
Prime Bank	Medium	Medium	Medium	Medium	Medium	Medium
African Banking Corporation	Small	Small	Small	Small	Small	Small
Consolidated Bank of Kenya	Small	Small	Small	Small	Small	Small
Credit Bank	Small	Small	Small	Small	Small	Small
Development Bank of Kenya	Small	Small	Small	Small	Small	Small
Dubai Bank Kenya	Small	Small	Small	Small	Small	Small
Equatorial Commercial Bank	Small	Small	Small	Small	Small	Small
Fidelity Commercial Bank	Small	Small	Small	Small	Small	Small
First Community Bank	Small	Small	Small	Small	Small	Small
Giro Commercial Bank	Small	Small	Small	Small	Small	Small
Guaranty Trust Bank Ltd	Small	Small	Small	Small	Small	Medium
Guardian Bank	Small	Small	Small	Small	Small	Small
Gulf African Bank	Small	Small	Small	Small	Small	Small
Habib Bank	Small	Small	Small	Small	Small	Small
Habib Bank A.G. Zurich	Small	Small	Small	Small	Small	Small
Jamii Bora Bank Ltd	Small	Small	Small	Small	Small	Small
K-Rep Bank	Small	Small	Small	Small	Small	Small
Middle East Bank (Kenya)	Small	Small	Small	Small	Small	Small
Oriental Commercial Bank	Small	Small	Small	Small	Small	Small
Paramount Universal Bank	Small	Small	Small	Small	Small	Small
Trans-National Bank	Small	Small	Small	Small	Small	Small
UBA Kenya Bank	Small	Small	Small	Small	Small	Small
Victoria Commercial Bank	Small	Small	Small	Small	Small	Small

Source: Secondary data 2014

## Note

- a. Large >5% market share; medium 5 < >1% market share; small <1% market share.
- b. Market share index is the composite of net assets, deposits, capital, number of loan accounts and number of deposit accounts.
- c. Charterhouse Bank Ltd is excluded since it has not been publishing results, as it is under receivership.

## Appendix E: Summary of Customer Base Growth

**Table E: Customer Base Growth of Kenya Commercial Banks Sector**

Bank name	Customer base increase (%)				
	2009	2010	2011	2012	2013
African Banking Corporation	8.84	15.25	26.33	4.82	28.37
Bank of Africa Kenya	54.43	115.12	38.90	41.54	20.70
Bank of Baroda (Kenya)	6.83	3.83	7.03	11.63	5.98
Bank of India	5.86	5.18	7.97	4.20	12.06
Barclays Bank of Kenya	18.42	15.23	18.41	11.07	9.33
CFC Stanbic Bank	12.75	21.48	31.63	1.20	16.72
Chase Bank (Kenya)	19.94	49.49	168.78	78.10	-35.53
Citibank N.A. Kenya	10.83	5.54	7.17	-48.54	-3.64
Consolidated Bank of Kenya	20.30	20.27	-18.86	25.05	0.13
Co-operative Bank of Kenya	39.76	49.58	28.83	24.33	-0.55
Credit Bank	-2.33	51.48	54.99	-7.67	16.48
Development Bank of Kenya	26.02	16.83	13.07	15.26	18.44
Diamond Trust Bank Kenya	16.59	16.72	25.02	42.71	85.79
Dubai Bank Kenya	12.72	126.58	1.96	13.85	12.90
Ecobank Kenya	62.95	-0.86	-35.34	114.21	69.48
Equatorial Commercial Bank	-71.23	284.65	7.48	23.28	21.62
Equity Bank	33.77	33.89	21.84	6.66	5.23
Family Bank	6.46	35.17	23.44	19.96	15.29
Fidelity Commercial Bank	21.66	29.43	8.13	18.89	2.26
First Community Bank	204.50	68.80	32.32	19.11	59.01
Giro Commercial Bank	24.67	13.53	6.07	-3.15	4.07
Guaranty Trust Bank Ltd	17.00	-10.47	-23.13	2.06	-0.29
Guardian Bank	2.76	-6.37	10.51	6.47	11.49
Gulf African Bank	391.14	-31.27	22.59	19.90	18.33
Habib Bank	-11.67	-1.07	-3.36	-1.91	-6.77
Habib Bank A.G. Zurich	0.99	-0.56	-3.93	-7.66	-1.74
I & M Bank	19.14	21.42	21.91	23.13	-72.68
Imperial Bank	20.95	33.15	27.36	23.73	18.04
Kenya Commercial Bank	48.59	78.35	23.29	-22.37	34.08
K-Rep Bank	127.46	-11.21	7.04	-22.27	9.23
Middle East Bank (Kenya)	-3.75	25.31	1.42	2.42	-5.41
National Bank of Kenya	23.84	15.61	11.38	6.96	9.99
NIC Bank	15.72	12.68	17.13	35.87	30.24
Oriental Commercial Bank	5.19	8.03	7.21	2.23	-1.59
Paramount Universal Bank	-41.14	38.19	-20.05	86.21	9.48
Prime Bank	11.53	10.16	28.65	23.98	12.94
Standard Chartered Bank Kenya	14.46	7.18	2.48	7.44	14.15
Trans-National Bank	19.17	27.98	29.40	23.91	8.02
UBA Kenya Bank	4.00	96.39	42.35	14.49	29.37
Commercial Bank of Africa Ltd	11.53	-3.70	27.80	2,949.00	431.60
Jamii Bora Bank Ltd	1.40	85,401.70	-8.70	-80.90	6.60
Victoria Commercial Bank	4.70	15.96	8.25	-5.71	2.33
<b>Aggregate Average</b>	<b>28.97</b>	<b>2,064.40</b>	<b>16.78</b>	<b>83.42</b>	<b>21.94</b>

Source; secondary data 2014

## Appendix F1: Summary of Profit before Tax Growth

**Table F1: Kenya Commercial Banks Profit Before Tax Percentage Growth**

Bank name	Profit before Tax Percentage Increase (%)				
	2009	2010	2011	2012	2013
African Banking Corporation	14.73	86.77	7.39	8.06	3.77
Bank of Africa Kenya	179.57	86.15	14.58	14.69	61.64
Bank of Baroda (Kenya)	14.69	151.79	-8.29	-0.56	50.27
Bank of India	0.00	62.73	-1.60	-37.75	106.43
Barclays Bank of Kenya	12.30	19.70	11.49	8.39	-8.44
CFC Stanbic Bank	1.52	57.84	48.69	50.62	48.66
Chase Bank (Kenya)	28.74	68.24	58.87	54.84	71.05
Citibank N.A. Kenya	-8.89	-5.76	66.79	50.54	-31.06
Commercial Bank of Africa	4.37	52.43	10.74	33.96	11.66
Consolidated Bank of Kenya	37.65	120.51	-4.44	-28.61	-180.68
Co-operative Bank of Kenya	11.69	49.15	10.95	55.23	11.81
Credit Bank	5.06	-59.04	50.82	57.96	-11.11
Development Bank of Kenya	9.94	25.53	-33.29	-33.94	163.46
Diamond Trust Bank Kenya	25.21	75.76	13.11	43.76	19.19
Dubai Bank Kenya	28.57	-66.67	592.33	-243.91	-153.53
Ecobank Kenya	-1817.91	-116.33	-35.43	-1363.42	-19.74
Equatorial Commercial Bank	-1062.50	-144.16	-309.35	-1021.61	-123.17
Equity Bank	17.09	67.18	29.98	32.69	13.53
Family Bank	-35.40	46.06	4.31	61.32	108.54
Fidelity Commercial Bank	-28.77	625.00	-20.02	-66.17	209.80
First Community Bank	-50.49	5.26	-169.77	163.37	-31.97
Giro Commercial Bank	46.83	242.70	-47.96	-37.26	85.02
Guaranty Trust Bank Ltd	-71.95	556.52	105.62	12.08	18.68
Guardian Bank	38.64	83.61	51.55	31.38	72.20
Gulf African Bank	-57.59	-129.01	230.60	140.70	16.04
Habib Bank	34.93	19.29	15.31	68.27	9.65
Habib Bank A.G. Zurich	18.18	-13.29	2.29	62.41	15.05
I & M Bank	8.15	71.46	48.38	5.94	28.34
Imperial Bank	19.17	55.61	30.74	17.18	30.44
Jamii Bora Bank	133.33	1100.00	-55.95	-243.24	69.81
Kenya Commercial Bank	19.13	79.55	22.05	11.89	12.63
K-Rep Bank	-38.77	-138.41	130.58	19.56	82.03
Middle East Bank (K)	46.67	368.18	-55.12	-49.17	72.34
National Bank of Kenya	20.14	24.97	-9.42	-53.07	55.10
NIC Bank	3.73	58.01	39.10	28.28	21.11
Oriental Commercial Bank	-51.47	454.55	5.25	-40.81	56.14
Paramount Universal Bank	-17.65	569.05	-59.86	-20.21	10.00
Prime Bank	22.61	36.52	40.35	7.43	63.05
Standard Chartered Bank (K)	42.83	14.01	7.60	39.61	15.60
Trans-National Bank	-27.27	80.68	85.47	9.19	-30.12
UBA Kenya Bank	-3650.00	-35.21	32.61	116.91	-29.96
Victoria Commercial Bank	27.06	43.98	6.01	48.93	19.35
<b>Aggregate</b>	<b>12.66</b>	<b>50.56</b>	<b>19.50</b>	<b>20.47</b>	<b>16.09</b>

Source; secondary data

## Appendix F2: Summary of Return on Asset Percentage Growth

**Table F2: Kenya Commercial Banks ROA Percentage Growth**

Bank name	ROA Percentage Growth (%)					
	2008	2009	2010	2011	2012	2013
African Banking Corporation	3.30	2.82	4.67	4.12	2.90	2.90
Bank of Africa Kenya	0.70	1.53	1.81	1.43	1.30	2.00
Bank of Baroda (Kenya)	3.40	3.24	5.65	4.57	3.60	4.80
Bank of India	5.00	3.91	5.04	4.18	2.40	4.10
Barclays Bank of Kenya	4.70	5.30	6.24	7.18	7.00	5.80
CFC Stanbic Bank	1.50	1.35	1.96	2.23	3.50	4.10
Chase Bank (Kenya)	2.40	2.42	2.45	2.33	2.70	2.90
Citibank N.A. Kenya	7.00	5.92	4.64	6.43	10.40	7.00
Commercial Bank of Africa	3.30	3.00	4.24	3.58	4.00	3.60
Consolidated Bank of Kenya	1.50	1.54	2.46	1.61	1.00	-0.80
Co-operative Bank of Kenya	3.70	3.26	3.61	3.68	4.80	4.70
Credit Bank	2.10	2.15	0.74	0.95	1.30	1.00
Development Bank of Kenya	2.60	2.27	2.22	1.37	0.80	1.80
Diamond Trust Bank Kenya	3.10	3.44	4.90	4.19	4.90	4.90
Dubai Bank Kenya	0.30	0.41	0.18	0.90	-1.20	0.50
Ecobank Kenya	0.50	-7.13	0.70	0.45	-4.80	-3.30
Equatorial Commercial Bank	-0.20	1.69	-0.32	0.55	-4.60	1.00
Equity Bank	6.10	5.66	6.95	6.84	7.40	7.70
Family Bank	5.00	2.50	2.48	2.01	2.70	4.00
Fidelity Commercial Bank	1.70	0.94	4.59	2.79	0.90	2.50
First Community Bank	-9.60	-3.42	-2.50	1.28	2.90	1.80
Giro Commercial Bank	2.00	2.63	6.20	2.79	1.70	2.80
Guaranty Trust Bank Ltd	0.80	0.18	1.07	2.12	2.00	1.60
Guardian Bank	0.70	0.83	1.39	1.92	1.90	3.00
Gulf African Bank	-7.60	-2.10	0.49	1.20	2.80	2.70
Habib Bank	3.20	4.16	4.34	4.62	6.50	6.20
Habib Bank A.G. Zurich	3.60	3.85	3.05	2.91	4.20	4.30
I & M Bank	4.40	3.94	4.80	5.80	5.20	5.50
Imperial Bank	4.90	5.09	6.43	6.37	5.50	5.80
Jamii Bora Bank	-0.50	-1.26	-4.85	-1.79	1.50	1.30
Kenya Commercial Bank	3.00	3.57	5.17	4.98	5.20	5.50
K-Rep Bank	-5.60	-3.76	1.44	2.75	3.20	4.20
Middle East Bank (K)	0.90	1.37	5.11	1.99	0.80	1.40
National Bank of Kenya	4.00	4.13	4.49	3.56	1.70	1.90
NIC Bank	3.40	3.30	4.41	4.57	4.20	4.60
Oriental Commercial Bank	2.50	0.97	4.01	3.83	1.80	2.50
Paramount Universal Bank	1.40	1.23	6.35	2.39	1.20	1.20
Prime Bank	2.30	2.33	2.37	3.07	2.70	3.80
Standard Chartered Bank (K)	4.70	5.39	5.37	5.03	5.90	6.00
Trans-National Bank	3.30	2.36	3.33	4.05	3.70	2.30
UBA Kenya Bank	0.10	-17.47	-5.85	-5.72	-13.60	-7.50
Victoria Commercial Bank	3.80	4.22	5.00	4.31	4.80	4.30
<b>Aggregate mean</b>	<b>1.99</b>	<b>1.61</b>	<b>3.02</b>	<b>2.94</b>	<b>2.54</b>	<b>3.01</b>

Source: secondary data 2014

### Appendix F3: Summary of Return on Equity Percentage Growth

**Table F3: Kenya Commercial Banks ROE Percentage Growth**

Bank name	ROE Percentage Growth (%)					
	2008	2009	2010	2011	2012	2013
African Banking Corporation	23.20	22.45	29.46	30.28	26.40	23.60
Bank of Africa Kenya	5.60	10.35	16.45	11.87	12.70	15.70
Bank of Baroda (Kenya)	33.10	28.30	38.52	33.96	28.90	33.10
Bank of India	36.00	29.43	35.94	28.87	14.90	24.60
Barclays Bank of Kenya	39.20	37.18	34.25	41.11	44.00	36.80
CFC Stanbic Bank	18.40	16.37	20.96	30.82	26.00	31.30
Chase Bank (Kenya)	29.30	26.00	31.20	28.62	25.80	30.10
Citibank N.A. Kenya	36.50	27.58	22.34	31.77	41.70	31.20
Commercial Bank of Africa	34.20	27.96	36.06	30.04	34.30	32.50
Consolidated Bank of Kenya	10.00	12.62	17.45	17.18	11.20	-11.50
Co-operative Bank of Kenya	23.90	23.14	27.52	29.41	33.10	30.00
Credit Bank	11.90	11.40	3.55	5.35	6.90	5.90
Development Bank of Kenya	13.90	13.79	15.85	10.08	6.30	15.00
Diamond Trust Bank Kenya	24.50	26.09	35.64	31.34	31.40	30.00
Dubai Bank Kenya	1.60	1.94	0.56	2.92	-3.30	1.50
Ecobank Kenya	3.80	-53.58	3.76	7.03	-76.70	-36.30
Equatorial Commercial Bank	-1.20	10.55	-3.70	5.91	-90.80	11.10
Equity Bank	24.20	23.87	32.90	34.53	37.60	36.00
Family Bank	34.10	18.51	16.01	15.72	17.40	29.50
Fidelity Commercial Bank	17.10	10.61	46.99	29.64	8.60	22.40
First Community Bank	-39.60	-22.93	-28.24	13.34	27.30	16.60
Giro Commercial Bank	20.70	21.59	47.35	20.90	11.70	18.40
Guaranty Trust Bank Ltd	7.00	1.92	11.32	20.22	13.90	6.80
Guardian Bank	5.30	6.99	11.77	15.94	18.30	25.70
Gulf African Bank	-30.00	-14.09	3.84	11.78	23.90	16.10
Habib Bank	23.60	26.37	26.24	25.51	33.80	30.00
Habib Bank A.G. Zurich	31.20	29.85	22.15	19.82	26.90	25.70
I & M Bank	31.20	23.62	23.15	32.17	28.50	29.50
Imperial Bank	35.20	35.69	40.31	44.28	42.00	43.60
Jamii Bora Bank	-0.90	-2.22	-8.19	-2.43	2.50	4.00
Kenya Commercial Bank	26.90	28.69	28.23	31.18	29.80	28.40
K-Rep Bank	-41.80	-26.11	9.55	19.23	20.10	29.80
Middle East Bank (K)	3.40	4.87	20.01	8.40	4.20	6.90
National Bank of Kenya	28.90	27.30	27.17	23.37	11.00	15.00
NIC Bank	26.70	23.76	30.60	33.95	28.60	29.60
Oriental Commercial Bank	7.20	3.36	16.07	14.93	8.20	11.70
Paramount Universal Bank	10.40	7.97	35.78	11.00	7.90	8.10
Prime Bank	15.00	18.40	19.74	28.88	27.80	32.50
Standard Chartered Bank (K)	41.30	48.71	37.94	40.11	37.60	37.00
Trans-National Bank	9.80	6.64	10.29	16.92	17.60	12.00
UBA Kenya Bank	1.10	-21.39	-15.54	-25.19	-32.60	-26.20
Victoria Commercial Bank	22.30	23.10	28.19	26.32	24.10	23.20
<b>Aggregate mean</b>	<b>15.58</b>	<b>13.73</b>	<b>20.46</b>	<b>21.12</b>	<b>15.46</b>	<b>19.45</b>

Source: secondary data 2014

## Appendix G: Multiple regression and Hierarchical Multiple Regression

**Model Summary<sup>b</sup>**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.747 <sup>a</sup>	.557	.507	.42206

a. Predictors: (Constant), managerial choices, Banks activities, initial conditions, Bank activity drivers

b. Dependent Variable: performance

**ANOVA<sup>a</sup>**

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	7.851	4	1.963	11.018	.000 <sup>b</sup>
	Residual	6.235	35	.178		
	Total	14.086	39			

a. Dependent Variable: performance

b. Predictors: (Constant), managerial choices, Banks activities, initial conditions, Bank activity drivers

**Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.374	.807		-.464	.646
	Banks activities	.416	.190	.356	2.185	.036
	Bank activity drivers	.525	.188	.471	2.787	.009
	initial conditions	-.198	.165	-.154	-1.203	.237
	managerial choices	.333	.161	.234	2.065	.046

a. Dependent Variable: performance

**Model Summary<sup>c</sup>**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.747 <sup>a</sup>	.557	.507	.42206	.557	11.018	4	35	.000
2	.767 <sup>b</sup>	.589	.529	.41266	.032	2.613	1	34	.115

a. Predictors: (Constant), managerial choices, Banks activities, initial conditions, Bank activity drivers

b. Predictors: (Constant), managerial choices, Banks activities, initial conditions, Bank activity drivers, dynamic capabilities

c. Dependent Variable: performance

ANOVA<sup>a</sup>

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	7.851	4	1.963	11.018	.000 <sup>b</sup>
	Residual	6.235	35	.178		
	Total	14.086	39			
2	Regression	8.296	5	1.659	9.743	.000 <sup>c</sup>
	Residual	5.790	34	.170		
	Total	14.086	39			

a. Dependent Variable: performance

b. Predictors: (Constant), managerial choices, Banks activities, initial conditions, Bank activity drivers

c. Predictors: (Constant), managerial choices, Banks activities, initial conditions, Bank activity drivers, dynamic capabilities

Coefficients<sup>a</sup>

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.374	.807		-.464	.646
	Banks activities	.416	.190	.356	2.185	.036
	Bank activity drivers	.525	.188	.471	2.787	.009
	initial conditions	-.198	.165	-.154	-1.203	.237
	managerial choices	.333	.161	.234	2.065	.046
2	(Constant)	-.237	.793		-.299	.767
	Banks activities	.313	.196	.269	1.595	.120
	Bank activity drivers	.441	.191	.396	2.309	.027
	initial conditions	-.257	.165	-.200	-1.560	.128
	managerial choices	.329	.157	.231	2.086	.045
	dynamic capabilities	.220	.136	.251	1.616	.115

a. Dependent Variable: performance

## Appendix H: Research Authorization Documents



### KENYATTA UNIVERSITY GRADUATE SCHOOL

E-mail: [kubps@yahoo.com](mailto:kubps@yahoo.com)  
[dean-graduate@ku.ac.ke](mailto:dean-graduate@ku.ac.ke)  
 Website: [www.ku.ac.ke](http://www.ku.ac.ke)

P.O. Box 43844, 00100  
 NAIROBI, KENYA  
 Tel. 810901 Ext. 57530

#### Internal Memo

FROM: Dean, Graduate School

DATE: 16<sup>th</sup> September, 2014

TO: Mr. Julius Kahuthia Mwangi  
 C/o Business Administration Dept.  
 KENYATTA UNIVERSITY

REF: D86/CTY/21732/10

#### SUBJECT: APPROVAL OF RESEARCH PROPOSAL

We acknowledge the receipt of your revised Research Proposal as per recommendations raised by the Graduate School Board of 13<sup>th</sup> August, 2014.

You may now proceed with your Data collection, subject to clearance with the Principal Secretary, Higher Education, Science and Technology.

As you embark on your data collection, please note that you will be required to submit to Graduate School completed supervision Tracking Forms per semester. The form has been developed to replace the progress Report Forms. The Supervision Tracking Forms are available at the University's Website under Graduate School webpage downloads.

Thank you.

JOSEPHINE KENDI  
 FOR: DEAN, GRADUATE SCHOOL

c.c. Chairman, Business Administration Dept.

Supervisors:

1. Dr. Muathe SMA  
 C/o Business Administration Dept.  
 KENYATTA UNIVERSITY
2. Dr. Mugambi G.K.M  
 Department of Marketing & Management Science  
 School of Business & Economics  
 Moi University  
 C/o Business Administration Dept.

JK/cao



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NAIROBI-KENYA

Ref: No.

Date:

**8<sup>th</sup> October, 2014**

**NACOSTI/P/14/1442/3544**

Julius Kahuthia Mwangi  
Kenyatta University  
P.O. Box 43844-00100  
**NAIROBI.**

**RE: RESEARCH AUTHORIZATION**

Following your application for authority to carry out research on *“Drivers of competitive advantage and performance of Commercial Banks in Kenya,”* I am pleased to inform you that you have been authorized to undertake research in **Nairobi County** for a period ending **31<sup>st</sup> December, 2014.**

You are advised to report to **the Chief Executive Officers of selected Commercial Banks, the County Commissioner and the County Director of Education, Nairobi County** before embarking on the research project.

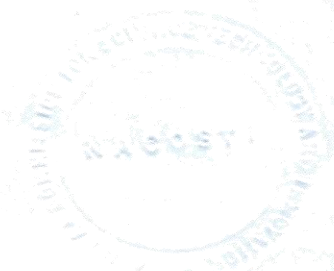
On completion of the research, you are expected to submit **two hard copies and one soft copy in pdf** of the research report/thesis to our office.

  
**DR. S. K. LANGAT, OGW  
FOR: SECRETARY/CEO**

Copy to:

The Chief Executive Officers  
Selected Commercial Banks.

The County Commissioner  
The County Director of Education  
Nairobi County.



**THIS IS TO CERTIFY THAT:**  
**MR. JULIUS KAHUTHIA MWANGI**  
**of KENYATTA UNIVERSITY, 0-100**  
**NAIROBI, has been permitted to conduct**  
**research in Nairobi County**

**Permit No : NACOSTI/P/14/1442/3544**  
**Date Of Issue : 8th October, 2014**

**Fee Received : Ksh 2,000**

**on the topic: DRIVERS OF COMPETITIVE**  
**ADVANTAGE AND PERFORMANCE OF**  
**COMMERCIAL BANKS IN KENYA**

**for the period ending:**  
**31st December, 2014**

*[Signature]*  
**Applicant's**  
**Signature**

*[Signature]*  
**Secretary**  
**National Commission for Science,**  
**Technology & Innovation**