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**THE RELATIONSHIP BETWEEN OUTSOURCING MANAGEMENT OF
AUTOMATED TELLER MACHINES AND ORGANIZATIONAL
PERFORMANCE AT THE COOPERATIVE BANK OF KENYA**

BY

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DECLARATION

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

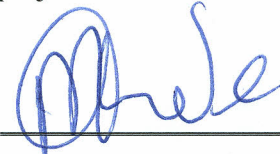
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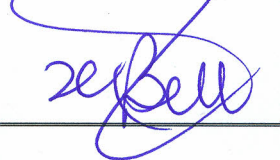
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DEDICATION

This work is dedicated to my brother Stephen Wakaba and my sister Milkah Mwaura, without whose caring support it would not have been possible, and to my parents Jane Wanjiku and Moffat Njoroge Wakaba who have always been passing to me the respect and value of education. To my bonus mum and dad: Jane & Felix DeSouza for their continuing support.

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ABSTRACT

Outsourcing is a business process term for what has literally become known as hiring a consultant, independent contractor, or freelancer to do a specific task or tasks for an organization in which the organization does not have either the time or the expertise to do on their own. Banks in Kenya dedicate considerable financial and management resources to the ongoing operation and support of their ATM channel. In recent years, most banks have been taking a closer look at alternative ways of managing their ATM networks. As banks work to minimize costs in the current global economic environment, one key way of achieving long-term and sustainable success is through the outsourcing and maintenance of a bank's ATM services.

The purpose of this study was to examine the relationship between outsourcing of management of ATM services and the organizational performance. The study shall adopt a descriptive survey design. The population studied was all the Co-op bank branches in Nairobi area. The branches were clustered based on their geographical location in Nairobi. Sampling was done using Stratified Random Sampling method. The instrument used for data collection was a questionnaire. Data collected was by use of descriptive and inferential statistics. Frequency tables, averages and percentages were used for data analysis and then the data was presented using tables, graphs and charts.

The key findings of this study is that by outsourcing ATM management to specialist organizations, Cooperative bank may better focus on their most value-creating activities, thereby maximizing the potential effectiveness of those activities. In addition, as outsourcing increases, costs may decline, and investment in facilities, equipment, and manpower can be reduced. The conclusion of the study is that contracting out is now broadly becoming an attractive option, its specific impact on the bank's performance, i.e. outsourcing result, has been well confirmed by research. The recommendations from this study is that the bank should consider outsourcing the remaining ATMs managed by the branches countrywide in order to further reduce their ATM maintenance expenses, to improve their ATM operations and to achieve a competitive advantage over other banking institutions thereby improving overall organization performance.

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ABBREVIATIONS

Co-op Bank	- Cooperative Bank of Kenya
ICT	- Information Communication Technology
ATM	- Automated Teller Machine
PBD	- Personal Banking Department
HR	- Human Resource
BOD	- Board of Directors
BOM	- Board of Management
SACCO	- Savings and Credit Cooperative
CEO	- Chief Executive Officer
DEPT	- Department
EFT	- Electronic Funds Transfer
RFP	- Request for Proposal
R&D	- Research and Development
IT	- Information Technology
SLA	- Service Level Agreement

DEFINITION OF TERMS

In this section, operational definitions are presented as used within the context of this research project.

Change management

A structured approach to shifting or transitioning individuals, teams, and organizations from a current state to a desired future state. It is an organizational process aimed at helping employees to accept and embrace changes in their current business environment.

Reengineering

Fundamental rethinking and radical redesign of business process to achieve dramatic improvements in critical measures of performance such as cost, service, and speed

Business Process Outsourcing

Business process outsourcing (BPO) is a division of outsourcing that involves the contracting of the operations and responsibilities of specific business functions (or processes) to a third-party service provider.

Electronic Funds Transfer

An electronic funds transfer (EFT) refers to computer-based systems used to perform financial transactions electronically. An EFT may be initiated by a cardholder when a payment card such as a credit card or debit card is used. This may take place at an automated teller machine (ATM) or point of sale (POS), or when the card is not present, for instance when the card is used for internet purchases.

Vendor

A vendor is anyone who provides goods or services to an organization or individuals. A vendor often manufactures inventorable items, and sells those items to a customer. Vendors may or may not function as distributors of goods. They may or may not function as manufacturers of goods. If vendors are also manufacturers, they may either build to stock or build to order.

Problem

Problem is the future state to be realized, some current state to be left behind and some organized process for getting from one state to the other.

Corporate Strategy

It's an elaborate long term detailed plan of a organization that indicate the direction of development and the objectives to be attained, together with the resources to be used to attain them.

Branch

Any retail location of a bank, its agency, additional office or any branch place of business located in any city or town in the country at which deposits are received, cheques are paid or money lent.

Innovation

Innovation is the successful use of skills and resources to create new technologies or new products and services.

Switching costs

The negative costs that a business incurs resulting from changing suppliers, brands or products. Most prevalent switching costs are monetary in nature, also effort- and time-based.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Outsourcing is defined by Chase *et al* (2004) as an “act of moving some firm’s internal activities and decision responsibilities to outside providers.” Lankford and Parsa (1999) similarly state “outsourcing is defined as the procurement of products or services from sources that are external to the organization”. Beyond legitimizing historical context of sub-contracting, there are many reasons why outsourcing has become an important planning activity in business. There are strategic and economic reasons and important trends, which make outsourcing a critical factor for present and future business success. Outsourcing as a key business strategy has been used by firms in various industries for many decades. Firms have been outsourcing business services, manufacturing operations and sometimes whole business lines successfully for a long time now. Business processes such as information technology (IT), logistics, payroll and human resources (HR) management are among the common processes regularly outsourced in most of the industries. Outsourcing of core functions like engineering, research and development (R&D), manufacturing and marketing are being considered by corporations. Competitive pressures and the need for enhanced financial, operational and strategic performance are driving an increase in the nature, scope and scale of outsourcing across companies worldwide.

The trading companies during the early part of the Nineteenth century practiced the outsourcing process. They used to outsource their non-core functions to some external companies, which were specialized in service, manufacturing ancillaries or components, or carrying forward certain functions for any product or service. The nature of outsourcing is diverse. Some firms now outsource core production activities so extensively that they no longer engage in production, as traditionally understood (Knemeyer *et al.*, 2003, Zsidisin, 2003). Other firms are extensively outsourcing secondary value-chain activities such as Information technology, human resource management, accounting systems, customer care and R&D (Johnson and Schneider, 1995; Lacity and Willcocks, 1998; Odagiri, 2003; Ono, 2003).

One reason why outsourcing is a critical issue is its position in the organization's decision making structure i.e. relationship of strategic, tactical and operational decision making. Structurally, outsourcing has changed from a tactical decision i.e. medium-term subcontracting of a small portion of an organization's unit production to a strategic decision of long-term subcontracting of a major portion of a firm's production, administration and service departments. While acknowledging that outsourcing is not a new concept, Yang and Huang (2000) point out that strategic outsourcing is relatively recent. All business organizations develop strategies by setting long-term goals as a general guide to their business operations. The strategic objective of outsourcing decision makers should seek to maximize the net benefits of outsourcing relative to the in-house provision of value-chain activities. In practice, this can often be simplified to minimizing the total costs of any given quantity and quality of outsourced goods or services (Barrar and Gervais, 2006). Business processes outsourcing is increasingly being used as a means of cost reduction and to also achieve business strategic goals (Basle Committee, 2005). Banking institutions globally have realized that outsourcing some of its processes create the potential to maximize profits while focusing on their customers and remaining competitive in the global market.

The first ATM services were introduced in Kenya by Standard Chartered bank in 1989 (Mwangi, 1998) , other major Banks like Barclays and Kenya commercial bank followed suit and in 1998 the country had 78 ATMs installed in different locations by different financial institutions. There was need to install more ATMs hence these banks started looking at the possibility of installing ATMs in off premise locations and outsourcing the management of these offsite ATMs. Co-operative Bank of Kenya is one of the many financial institutions in Kenya which has outsourced some of its ATMs to third party firms for management of the ATMs operations. As many banks customers interact mostly with their bank via the ATM, an extensive ATM fleet can be an important competitive differentiator. The need for banks to bring the ATMs closer to the customer to improve performance is one of the reasons why they consider outsourcing ATMs management

1.1.1 The Strategy of Outsourcing

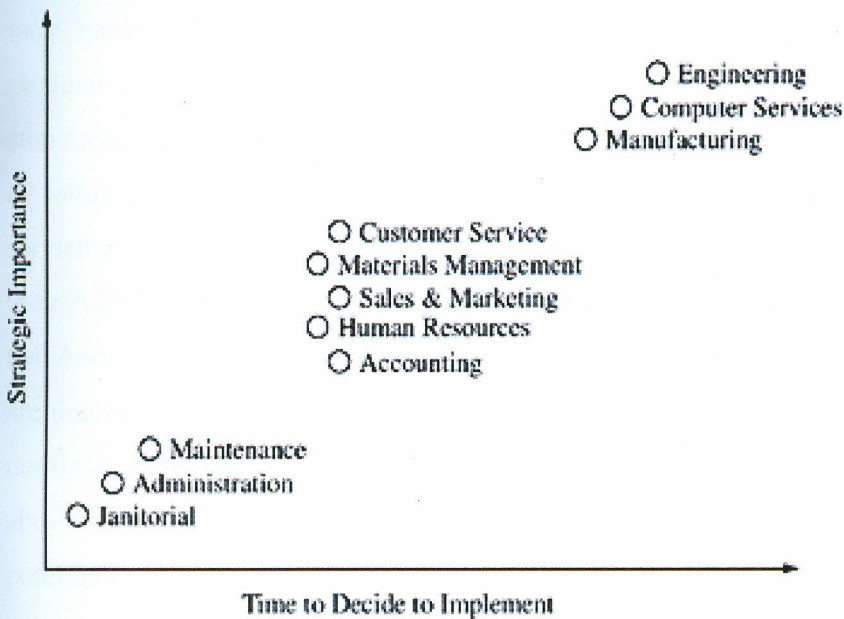
According to Bragg (2006) before deciding to outsource any business function or activity, most banks consider the underlying reasons why outsourcing is being considered in the first place. It may be due to a deeper problem may be that the function in question is not doing a good job of trumpeting its accomplishments, or of showing management that the cost of keeping the function in-house is adequately offset by the resulting benefits. In these cases, it may do no good to outsource the function because management may be replacing a perfectly adequate in-house staff that is not good at publicizing itself with a supplier who performs no better but who is quick to point out how much it is doing for the organization. If management suspects that this may be the reason why outsourcing is being considered, it is useful to bring in a consultant who can review the performance of the in-house employees and see if they are, in fact, doing a better job than they are saying.

Banks essentially have three kinds of processes: core processes which give strategic advantage, critical non-core processes which are important but not competitive differentiators, and non-core non-critical processes which are needed to make the environment work. Outsourcing non-core processes frees the bank's time and resources for core competencies. The people who ultimately make the outsourcing decision should also consider that it is not necessary to outsource an entire functional area; instead, they can cherry pick tasks within the function that are clearly worthy of being outsourced and keep all other tasks in-house. This reduces the risk of having the chosen outsourced organization do a bad job of handling its assigned tasks, since fewer tasks are at risk, and it allows the bank to hand over the remaining functional tasks to the provider as the bank management becomes more comfortable with their performance.

The typical outsourcing path that most companies follows starts with a function that has minimal strategic value and will not present a problem even if the outsourced organization does a poor job of providing the service. If the organization's experience with these low-end functions proves successful, then they will be more likely to advance to outsourcing those functions with more strategic value or with more business-threatening consequences if the provided service is inadequate. These functions include accounting, human resources, customer service, cheque clearing, ATMs management and logistics. Finally, if the organization continues to perform well

with all or part of these functions outsourced, it will consider moving to outsourcing the most important functions; typically, these are for instance computer services. This progression is shown on figure 1.1 below. Similarly, many banks experiment with outsourcing functions of low importance and later include functions with more strategic importance, depending on their earlier experience with the other functions.

Figure 1.1: Typical Outsourcing path (Bragg 1998)



1.1.2 Automated Teller Machines (ATMs)

According to Peter and Sylvia (2008), an ATM is an equipment used to make financial transactions which combines a computer terminal, recordkeeping system, and cash vault in one unit, permitting customers to enter a bank's bookkeeping system with either a plastic card containing a Personal Identification Number (PIN) or by punching a special code number into a computer terminal linked to the bank's computerized records 24 hours a day. Once access is granted, it offers several retail banking services to customers. They are mostly located outside of banks, and are also found at airports, malls, and places far away from the home bank of customers known as offsite or off-premise locations. They were introduced first to function as cash dispensing machines. However, due to advancements in technology, ATMs are able to

provide a wide range of services, such as making deposits, funds transfer between two or accounts and bill payments. Banks tend to utilize this electronic banking device, as all others for competitive advantage.

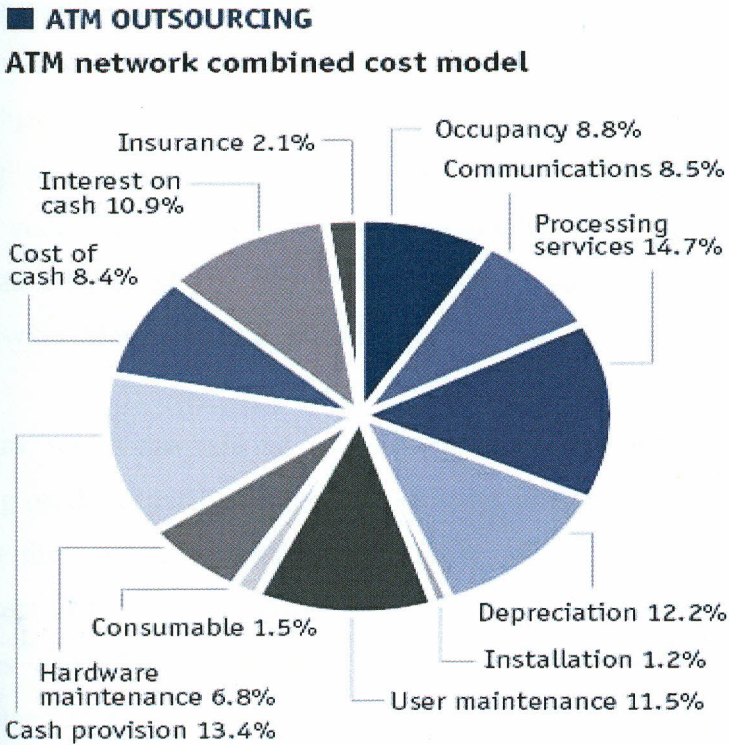
The combined services of both the Automated and human tellers imply more productivity for the bank during banking hours. Also, as it saves customers time in service delivery as alternative to queuing in bank halls, customers can invest such time saved into other productive activities. For most banks ATMs are a cost-efficient way of getting higher output as they realize higher productivity per period than human tellers do. ATMs continue to operate when human tellers stop therefore there is continual productivity for the banks even after banking hours. In addition, by automating services that were previously completed manually, ATMs reduce the costs of servicing some depositor demands. These potential benefits are multiplied when banks share their ATMs, allowing depositors of other banks to access their accounts through a bank's ATM (McAndrews, 2003). Banks have become the principal deployers of ATMs. Two reasons for this are that they want to increase their market share, although due to the prevalence of ATMs, it is not likely to be the primary means by which ATMs increase profitability for most banks; or/and above a certain level of operations, the cost of a single transaction performed at an ATM is potentially less than the cost of a transaction conducted from a teller, as ATMs are capable of handling more transactions per unit of time than are tellers (Laderman, 1990).

1.1.3 Outsourcing ATM management and the Banks Performance

Gilley and Rasheed (2000) proposes that organizational performance in firms improve because there is an increased focus on a firm's core competencies is an important benefit associated with outsourcing (Dess et al., 1995; Gilley and Rasheed, 2000; Kotabe and Murray, 1990; Venkatraman, 1997). The evolving literature on core competencies has been concerned with the "make-or-buy" decision that every firm faces. Should a bank manage their own ATMs in-house, or should it outsource these tasks to vendors that specialise in ATM management (Espino-Rodri'guez and Padro'n-Robaina, 2005; Taylor, 2005; Walker and Weber, 1987)? Ronald Coase (1937) first tackled this question 70 years ago in a classic article. His broad argument was similar to Adam Smith's: if an outside party can do the work more efficiently and inexpensively

than can the firm itself, then the outside party ought to do it: if the firm's employees can do the job better, then the work ought to remain in-house (Bahli, 2002; Espino-Rodríguez and Padro'n-Robaina, 2005; Taylor, 2005). According to the survey, conducted by Accenture and the Economist Intelligence Unit, two-thirds of the respondents – all of whom had been outsourcing a major business process for at least two years – agreed that outsourcers who know how to manage the process can enhance their company's performance and achieve a high level of satisfaction with the results (Lacey and Blumberg, 2005).

Figure 1.2



Source: Diebold

As shown in figure 1.2, there are several costs associated with operating ATMs, including cash replenishment and provision, insurance, processing, hardware/software maintenance and armoured car support services, therefore banks have the option to manage individual ATM services through separate service providers or to outsource the whole ATM management to one provider. Research shows that increased outsourcing of non-core activities can improve service quality (Dess et al., 1995). A vendor will be in a better position to provide the outsourced

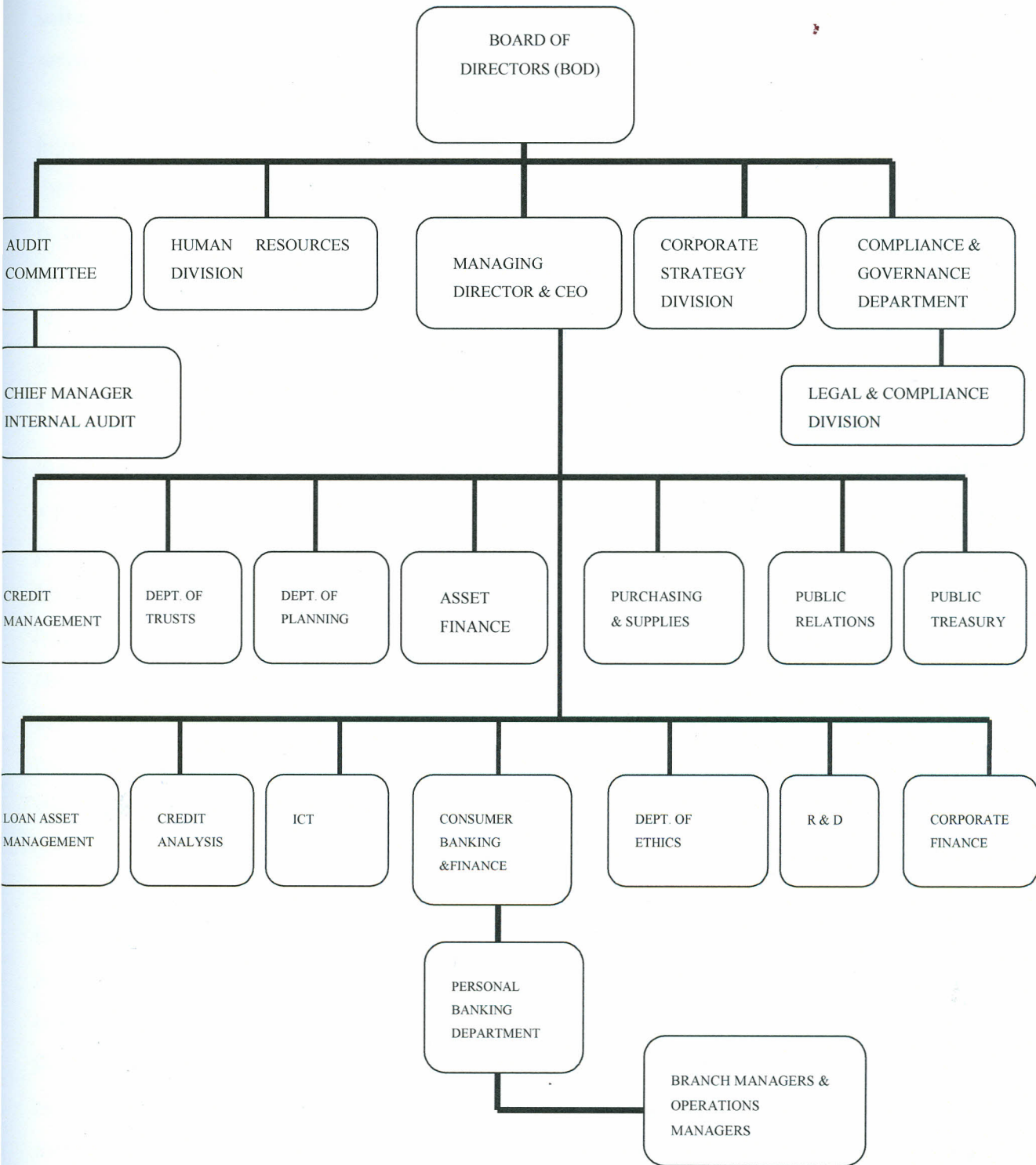
services because this area constitutes its core business (Gilley and Rasheed, 2000). Lastly, outsourcing ATM management activities with low strategic value can lead to lower costs and thereby improve the organizational results (Espino-Rodríguez and Padro'n-Robaina, 2005). Firms are increasingly viewing outsourcing strategies for reducing or controlling costs (Smith et al., 1998). Empirical research also suggests that outsourcing firms often achieve cost advantages relative to vertically integrated firms (Gilley et al., 2004; Gilley and Rasheed, 2000).

1.1.4 The Co-operative Bank of Kenya

Cooperative Bank of Kenya is one of the forty-four (44) licensed banks in the Kenya. The bank was registered as a co-operative society on the 19th June 1965. It did not however commence operations, as it was not registered under the Banking Act. In this status, it could not fulfil the main objective for its establishment, which was to mobilise financial resources and provide banking services to the co-operative movement. The Bank applied for a banking licence to operate under the Banking Act, which was granted later on in 1968. As of January 2012 Co-op bank had established 107 branches distributed countrywide & 447 operating ATMs installed countrywide (Management Report Circular, 2012).

The bank serves the banking needs of individuals, small businesses and large corporations, focusing on the needs of cooperative societies in Kenya. The bank ATMs provide many more services than simple dispensing cash. These ATMs have evolved from simple currency note dispensers to true mini branches where the customer can pay bills, verify checking account balances and obtain statements. Driven by the countrywide presence supported by an interconnected network of an expanding network of service outlets, Co-op bank personal banking department has been working to ensure that the bank continues to offer banking that is both affordable and convenient to individual customers while maintaining profitability. The Co-operative Bank has endeavoured to extend and develop its ATM fleet, offering advanced features to both its own and other banks' customers, to help attract more business and build new revenues. Figure 1.3 shows the current governance structure of Co-operative bank of Kenya.

Figure 1.3 Current governance structure for Co-operative Bank



Source: Co-operative Bank Annual report, 2008.

Co-op bank has been operating its fleet of ATMs on an internal platform for 15 years. During this time, it has continued to invest in its ATM network platform to support hardware and software upgrades. Throughout its history, Co-op bank has developed a bias against outsourcing services to third party providers. This bias was especially strong as it pertained to its ATM network since the bank has developed unique functionality for its machines. The management initially was unwilling to outsource due to risks involved. According to Aubert, et al., (1998) and Earl (1996), negative perceptions of outsourcing are often equated with risks of outsourcing, that is, the possibility of outsourcing failure. Over time the bank's ATM fleet has grown to over four hundred machines. Throughout this period of growth Co-operative bank was required to make regular investments in additional hardware to support its ATM network. Expecting future growth, the bank faced an important decision; continue to make expensive hardware and software purchases or consider outsourcing to a third party management provider.

In early 2000, Co-op bank management decided to outsource ATMs when it was confronted with a potentially large hardware and human capital investment which meant a decline in financial performance. The bank was operating sixty ATMs and was considering adding more machines. To support its expansion there was need to invest in expensive operating equipment. With its in-house operating platform already experiencing reliability issues, management was concerned about its ability to sufficiently sustain its growing fleet. In addition, the bank did not have staff members dedicated to supporting its ATM network. The problems of the in-house managed fleet, combined with the expense of supporting it, were taking a toll on the bank's management. Key staff members were becoming increasingly involved in the operations of the ATM fleet and were unable to dedicate themselves to the core competencies of the bank. As a result, the Co-operative bank management made a decision to contract ATM outsourcing providers for support. Since the bank was experiencing more and more reliability problems, it was clear that there was need to dedicate full-time staff employees to try and improve the level of service it was providing to its customers. The main outsourcing concern has been to serve customers more conveniently, and in the process improve performance by increasing profits and competitiveness. However no evidence has been provided for this bank and others in the Kenya industry to show how outsourcing of ATM management services has influenced the performance of organizations in the banking industry.

1.2 Problem Statement

Co-op bank has been outsourcing ATM management and still is. However the bank hasn't been able to clearly establish whether there is a relationship between outsourcing and the bank's performance. To date there has been no empirical study which has been carried out by the bank to establish whether this relationship exists (Co-op Bank Financial Results Quarter 3, 2010)

Despite its growing emphasis, the result is still vague and an unexplained puzzle (Jiang et al., 2006; Jiang and Qureshi, 2006). Thus, the uncertainty remains whether outsourcing is a myth or a reality from the perspective of organizational performance. Studies tend to concentrate on the reasons organizations outsource and how to outsource, and there are very few empirical studies that examine the impact of outsourcing on organizational performance in banks (Bolat and Yilmaz, 2007). This study presented new data and empirical insights into the relationship between outsourcing and organizational performance at Co-operative bank. The success of this study can therefore be imitated in studying outsourcing and organizational performance in other industries as well. Barako and Gatere (2008) researched on the outsourcing practices in the Kenyan banking industry, however their research failed to show whether there exists a relationship between outsourcing and performance of organizations in the banking industry.

1.3 Objective of the Study

The main objective of this study was to examine the relationship between outsourcing of ATM management services on the performance of Co-operative Bank of Kenya. The specific research objectives was to:

- i. Assess the relationship between ATM based financial considerations for outsourcing on the performance of the Co-operative bank of Kenya.
- ii. Examine the relationship between operational considerations for outsourcing ATM management on the performance of the Co-operative bank of Kenya.
- iii. Assess the relationship between bank business strategic considerations for outsourcing ATM management on the performance of the Co-operative bank of Kenya.

1.4 Research Questions

- i. How has the financial consideration for outsourcing ATM management been related to the performance of the Co-operative bank?
- ii. How has the operational consideration for outsourcing ATM management been related to the performance of the Co-operative bank?
- iii. How has the strategic consideration for outsourcing ATM management been related to the performance of the Co-operative bank?

1.5 Significance of the Study

Since the bank is still expanding its ATM fleet through the acquisition of more ATMs, this study will help Co-op bank management make the decision whether to continue outsourcing a fraction or its entire ATM fleet or manage the ATM processing in-house. This study will also improve literature on ATM outsourcing and management and its implication on bank's performance. This research is of significance to firms and consultants in other industries to provide data, which will assist these firms in making the outsourcing decision by clearly showing the impact outsourcing has on performance.

1.6 The Scope of the Study

This study was carried out at Co-operative Bank branches in Nairobi. The respondents targeted for this research were the people who have in-depth understanding of the planning and decision making process for ATMs acquisition, installations and managing the machines operations. This enabled the researcher to gather information that was more reliable and of acceptable accuracy. The study only focused on outsourcing of ATMs management services.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter begins by exploring the theories that are applied in outsourcing of ATMs management at Co-operative bank. The phases in the outsourcing process are also looked into, to give insight on the steps firms need to follow when they make the decision to outsource. Reasons that drive an organization to outsource are explored in depth. In this chapter, the three levels of outsourcing namely transformational, tactical and strategic and lastly are looked into. An empirical review of outsourcing strategies is explored to include variables both independent and dependent which are key to establishing the outsourcing to performance relationship. A conceptual framework to show the relationship between these variables is provided at the end of this chapter.

2.2 Theories of Outsourcing

Many theories have been utilized to help the academics to understand the nature of outsourcing, and to help practitioners successfully manage the process. From its occurrence, outsourcing has been approached by different theories (Perunović and Pedersen, 2007). Various authors identified significant number of theories that could explain the outsourcing phenomenon (Gottschalk and Solli-Sæther, 2005; McIvor, 2005). The theoretical perspectives presented below may help to understand outsourcing practices in different settings of this study.

2.2.1 Theory of Transaction Cost Economics

Transaction cost economics (TCE) has been the most utilized theory of outsourcing and is perceived to provide the best decision making tools to help organizations to decide to outsource and to prepare themselves for forthcoming outsourcing arrangements. The governance features of the theory influenced that it has been applied in studying the Managing relationship phase, whilst the concept of switching costs made the theory applicable in the reconsideration phase (Perunović, 2007). Another useful issue for outsourcing provided by TCE is explanation of contractual complexity. TCE theory is used to argue that all functions where benefits to the

company are greater than the transaction costs should be outsourced. Benefits include increased revenues and reduced costs.

2.2.2 Relational View

Relational view theory has been adopted in this study as well. This theory develops and explains how firms gain and sustain competitive advantage within inter-organisational relationships (McIvor, 2005). Its key premise – the concept of relational rents has been explored to explain how firms choose their future outsourcing partners and preferred type of the relationship. Perunović (2007) explains that this theory has been also utilized in studying the Transition, Managing relationship and Reconsideration phases. This makes the relational view the only theory that has been applied in the research of all the outsourcing process' phases.

2.2.3 Theory of Core Competencies

The concept of core competences was adopted in this study and it is developed on the basis of the resource-based theory. Prahalad and Hamel (1990) defined the core competencies as the collective learning in the organisation, especially how to coordinate diverse production skills and integrate multiple streams technologies. The application of concept of core competences in outsourcing became very popular among researchers. The concept has been predominantly use to develop and test various outsourcing decision frameworks arguing that the core activities shall remain in house. Learning and communication premises of the concept made it also applicable in the Managing relationship and Reconsideration phases. Vendor's competences are assumed to be one of the most important factors that influence success of an outsourcing arrangement (Levina and Ross, 2003; Feeney et al., 2005).

2.2.4 Resource-Based View Theory

The core premise of the resource-based view is that resources and capabilities can vary significantly across firms, and that these differences can be stable (Barney and Hesterly, 1996). If resources and capabilities of a firm are mixed and deployed in a proper way, they can create competitive advantage for the firm. The resource-based view in outsourcing builds from a proposition that an organisation that lacks valuable, rare, inimitable and organised resources and

capabilities, shall seek for an external provider in order to overcome that weakness. The essence of the resource-based theory of the firm lies in its emphasis on the internal resources available to the firm, rather than on the external opportunities and threats dictated by industry conditions. Firms are considered to be highly heterogeneous, and the bundles of resources available to each firm are different. This is both because firms have different initial resource endowments and because managerial decisions affect resource accumulation and the direction of firm growth as well as resource utilization (Løwendahl, 2000). The resource-based theory of the firm holds that, in order to generate sustainable competitive advantage, a resource must provide economic value and must be presently scarce, difficult to imitate, non-substitutable, and not readily obtainable in factor markets. This theory rests on two key points. First, that resources are the determinants of firm performance and second, that resources must be rare, valuable, difficult to imitate and non-substitutable by other rare resources. When the latter occurs, a competitive advantage has been created (Priem and Butler, 2001).

2.2.5 Agency Theory

The focus of the agency theory originally was on the relationship between managers and stakeholders (Jensen and Meckling, 1976), but had spread over the time on explaining the relationship between two inter-firm subjects. In that context we associate the agency theory to understanding the relationship between outsourcer and vendor. Sources of the agency problem, moral hazards and adverse selection (Arrow, 1985) should be resolved by monitoring and bonding (Barney and Hesterly, 1996). According to Eisenhardt (1985), agency theory is concerned with resolving two problems that can occur in agency relationships. The first is the agency problem that arises when the desires or goals of the principal and agent conflict and it is difficult or expensive for the principal to verify what the agent is actually doing. The second is the problem of risk sharing that arises when the principal and agent have different risk preferences. These problems are well known in outsourcing. An example might be that the client organization wants to reduce its costs, while the vendor organization wants to maximize profits. The agency problem arises when the two parties do not share productivity gains. The risk-sharing problem might be the result of different attitudes towards the use of new technologies. Given the difficulties of behavior-based contracts suggested by agency theory, it is reasonable to

assume that the overwhelming majority of clients would insist on outcome-based contracts (Gottschalk & Solli-Sæther, 2005)

2.2.6 Knowledge-based View theory

The knowledge-based view provides insight in understanding how individuals co-operate to produce goods and services. The knowledge-based view distinguishes two ways how knowledge is shared among partners. They are knowledge generation and knowledge application. The knowledge-based view has been used in utilized in the outsourcing research to prove that knowledge sharing in the Managing relationship phase is positively related to the success of an outsourcing arrangement.

Year	Authors	Theory	Method	Key points	Applicability to outsourcing process
1995	Lacity and Willcocks	Transaction Costs Economics (TCE)	Case study	Experiences to the TCE framework of efficient governance structures resulted in anomalies	P, VS, MR, R
1995	Willcocks and Choi	Relational view	Case study	Defining characteristics of total IT outsourcing strategic alliances and identifying problems of managing them	P, MR
1997	Brandes et al.	TCE, Core competences	Case study	Outcomes are more successful if outsourcing decision is based on core competence and cost efficiency and if outsourced unit is able to develop strong resource base	P, MR, R
2001	Lee	Knowledge-based view, Core competences	Survey	Knowledge sharing is positively related to outsourcing success	MR
2001	Roy and Aubert	RBV	Case study	The best predictor of success and failure is the governance mode and the position of project in the value matrix	P
2006	Barthélemy and Quelin	TCE, Resource-based view	Survey	To restrict vendor's opportunism, contracts must contain incentives and penalties, as well as pricing and monitoring clauses	P, VS, MR, R

Table 2.1 – Theories utilized in the outsourcing process

Table 2.1 shows some of previous papers and the theories utilized. The last column indicates phases of the outsourcing process each paper and its theoretical grounding have addressed. The abbreviations P, VS, T, MR, and R stand for the phases of the outsourcing process i.e., Preparation, Vendor(s) Selection, Transition, Managing relationship, and Reconsideration which are explored in the next topic of this study.

2.3 Theoretical Review of the Outsourcing Process

Outsourcing is the process of establishing and managing a contractual relationship with an external supplier for the provision of capacity that has previously been provided in-house (Momme, 2001). In spite of an impressive research intensity of the outsourcing process, there are only few frameworks depicting the actual stages and the layout of the overall process of outsourcing. Each of the phases has key activities, thus emphasizing the complexity of the outsourcing process and arguing for a need that it has to be managed carefully throughout all of its life cycle. The outsourcing framework is grouped into stages outlined in the following sequence:

2.3.1. Preparation

The first phase of the outsourcing process should reflect, as Shepherd (1999) calls it, the underlying philosophy of an outsourcing agreement. The philosophy of an outsourcing arrangement consists of the objectives of the principal architects of the agreement, along with the set of beliefs that led an organization to conclude that outsourcing would be an effective and appropriate way to proceed (Shepherd, 1999). Quinn and Hilmer (1994) coined the term “strategic outsourcing” to emphasise distinction between what is the strategic core of the firm and those other activities which are necessary to attain the firm's strategic goals. As Willcocks et al. (1995a) argue, taking a strategic approach to outsourcing means recasting the question “to outsource or not?” into a more useful question: “how do we use, if at all, the opportunity which is available on the market to leverage business advantage?” The issue then becomes not outsourcing, but rightsourcing.” In contrast to that, Greaver (1999) proposed as the first stage the formation of cross-functional teams to study and implement outsourcing initiatives. The project team should have really strong arguments to reject top management’s prior decision to outsource.

The major task in this phase is to explore strategic sourcing options, and a significant number of tools have been developed over the time to assist the management in making the right decision. The main debate is that organization should keep its core activities in-house, while those not important may be outsourced.

Alexander and Young (1996) suggest four meanings of core activities, as perceived by Companies i.e. traditionally performed activities, Activities critical to performance, Activities creating competitive advantage or Activities driving growth and renewal. Those activities enable competitive advantage, and should therefore be retained in-house. Cullen and Willcocks (2003) draw up the strengths and weaknesses of three outsourcing approaches: Big bang approach whereby significant portions of all activities are outsourced at one time, piecemeal approach where each activity is outsourced independently over time and a variety of suppliers are used and incremental approach where one or more suppliers are selected for pilot project(s) with a planned escalation of outsourcing. The escalation occurs if preceding outsourcing is successful.

When considering outsourcing as an option, organisation should decide early in the process what type of relationship with vendors would be the most suitable for it. The type of the relationship is usually determined by the importance of the activity that is to be outsourced, by existing risks on the vendor market, and by the amount of work outsourced. Ronan McIvor (2005) argues that when activities are critical to competitive advantage and the supply market risk is low, the organisation should deploy a competitive collaborative relationship strategy. If the supply market risk is high the strategy should be close collaborative. In the case when activities are not critical to the competitive advantage, organisations should deploy either adversarial or secure supply strategies, in cases of low and high supply market risk respectively. Franceschini and colleagues (2003) combine specificity and complexity, from the transaction cost economics, to determine four types of relationship: temporary relationship (high specificity-low complexity), traditional vendor (low specificity and complexity), strategic union (low specificity and high complexity), and network organisations (high specificity and complexity). Specificity refers to the level of reutilisation of the considered product/process for many different uses. Complexity refers to the difficulty of monitoring and defining contract terms and conditions of the outsourcing process. In

essence, an outsourcing organization will seek one of the two polarities of a relationship. It will strive either for a short-term transactional (contractual) or a long-term relational (collaborative) relationship. As a result of outsourcing more critical activities, organisations have been attempting to develop collaborative relationships with suppliers as they seek to reduce the risks associated with outsourcing (McIvor, 2005). According to Greaver (1999), longer contracts tend to be used when the relationship is strategic, outsourced functions and processes are closer to the core competences, significant assets are transferred to the vendor and when the vendor has to make significant investments. Shorter contracts are preferred when significant uncertainties are involved, the relationship is not strategic, outsourced functions and processes are clearly non-core, assets being transferred are not significant and when the vendor will invest little in start-up costs

2.3.2. Vendor(s) Selection

Vendor selection has become an increasingly important phase of the outsourcing process. This importance stems from a tendency of outsourcing organisations to engage in more collaborative and relational oriented outsourcing arrangements (McIvor, 2005). If vendor scanning activities from the preparation phase haven't revealed the final candidate for entering the negotiation process, then vendor selection shall be carefully designed. It shall follow a more or less pre-determined path, consisting of writing the request for proposals (RFP), determining evaluation criteria, evaluating and selecting the vendor, negotiating and finalising the contract. The outsourcing organization shall choose partner(s) that it will be tied to for a period of time. This phase shall provide the major output, the contract. Outsourcing contracts may be developed as a single term (fixed one-term), rollover (extendable) or evergreen contracts (Cullen and Willcocks, 2003). The outsourcing contract is the only certain way to ensure that expectations are realised. It may comprise standard elements, although each outsourcing arrangement shall take into account specificities of parties involved and characteristics of the work that is about to be outsourced. An outsourcing contract will include some of the following (McIvor, 2005): Service Level Agreement, Transfer of staff and assets, Price and payment terms, Liability, Contract termination and Flexibility. Flexibility of contracts is an emerging characteristic of contracts, which is being explained by the theory of incomplete contracting. The robustness of the contract is very

important and it should serve as an effective mechanism in the case of activities for which complete information exists and future uncertainty is manageable. Ronan McIvor (2005) illustrates numerous methods of incorporating flexibility into a contract through incomplete contracting, thus ensuring that the outsourcer is not locked into a relationship with an uncompetitive partner. These mechanisms include Price flexibility, Renegotiating, Contract length, Early termination. The vendor(s) selection phase should provide an answer on the question: To whom to outsource.

2.3.3. Transition

Having decided to outsource, specified the outsourcing arrangement, chosen the vendor and signed the contract, the outsourcer has to finally ensure that it really has let go of its function, process, product, and/or service. The transition phase makes all planned activities start happening. Its goal is to secure efficient mobilisation (Cullen and Willcocks, 2003). The transition phase is typically focused around transferring assets, people, contracts, hardware and software, information and projects that the vendor will have responsibility for in the future (Greaver, 1999; Cullen and Willcocks, 2003). This process embraces change management. The performance of the transition phase may be measured by the ability to implement the change process (Momme, 2001). Click and Duening(2005) explain that an effective change management process requires a compelling vision of the outcome of the change process, a visible leadership from top management of organisation, an extensive communication and opportunities for employee feedback, the ability to deal with job loss and changeover and also the ability to maintain business continuity and benchmark performance.

Regardless of whether the process remains on-site or is moved off-site, there will be a need to transfer process-related information, knowledge, and controls. In addition, during the transition phase it will be necessary to establish information exchange and data interface protocols that mesh the existing standards and information management architectures of each firm (Click and Duening, 2005). A very sensitive topic is how to handle employees who need to move to the vendor, or those whose employment is going to be terminated. The workflow has to undergo

substantial reengineering and establishment of new interfaces (Momme, 2001; Cullen and Willcocks, 2003), since some activities are performed in the new setting. Therefore, internal protocols and procedures need to be specified.

2.3.4. Managing Relationship

The outsourcer and vendor may be engaged in four generic types of relationships (Pinnington and Woolcock, 1997): reciprocal, client dominant, vendor dominant, or preferred vendor. Some relationships may evolve over time, from short-term contractual obligations, to even strategic alliances (Willcocks and Choi, 1995), although only in case of total outsourcing arrangements. An outsourcing relationship may be maintained in three ways: through contracts, by trust or by hostages (Willcocks and Choi, 1995; Barthélemy, 2003). Barthélemy (2003) distinguishes four types of managing relationship based on soft and hard outsourcing management styles. The soft side of outsourcing management refers to the development of relationships based on trust. Trust can be defined as the expectation that the vendor will not take advantage of the client or *vice versa*, even when the opportunity is available. The hard side of outsourcing management refers to development and enhancement of a good contract. Companies achieve most satisfactory outcomes of outsourcing if they complementarily manage by implementing both hard and soft techniques.

This phase shall facilitate the success of the outsourcing project, provide added value, establish deeper trust and relationship with partner(s), trace future steps, and secure the organization against contractual breaches. The outsourcer has to establish communication, information and knowledge sharing, and monitoring systems in order to secure a successful outsourcing relationship with its partner, and a successful outsourcing arrangement in general. The degree of knowledge sharing will have a positive effect on the outsourcing process (Lee, 2001). The influence of knowledge sharing on the outsourcing success is moderated by the level of organisational capability and the quality of the partnership. The outsourcing process will be slower and more costly, the less participants are capable and willing to articulate and share their knowledge with the external vendor (Mahnke, 2001). Critical to success of outsourcing is

effective communication among all parties, based on a collaborative relationship. Relationship management is an integral part of each governance model and can be performed on the strategic, functional and operational levels (Gewald and Helbik, 2006).

2.3.5. Reconsideration

In this phase organizations are challenged to provide the answer to the question of what now? Reconsideration is an almost completely neglected phase of the outsourcing process, except in few examples. The outsourcing contract can be terminated before expiring as the result of changes in control of the supplier, for convenience, due to insolvency, offence, breach, or default (Cullen and Willcocks, 2003). Sometimes it is not necessary to have a particular reason for terminating the contract. It is called voluntary termination. The third option is the pure expiration of contract. Outsourcers should use this time to put together two and two and see whether they have achieved success or they have failed, and to decide what they shall do now. According to Cullen and Willcocks (2003), there are possible options such as either to continue with outsourcing with the same partner or continue with outsourcing with re-tendering the supplier(s)

In buyer-supplier relationships, switching costs are defined as the overall cost or difficulty of switching i.e., additional costs and efforts in changing suppliers (Whitten and Wakefield, 2006). Switching costs are further divided into the following costs: uncertainty costs, post-switching behavioural and cognitive costs, set-up costs, hiring and retraining costs, management system upgrade costs, lost benefit costs, search and evaluation costs, and finally, sunk costs (Whitten and Wakefield, 2006).

2.3.6 Drivers of Outsourcing

Greaver (1999) defines outsourcing as the act of transferring some of an organization's recurring internal activities and decision rights to outside providers, as set fourth in a contract. Because the activities are recurring and a contract is used, outsourcing goes beyond the use of consultants. As a matter of practice, not only are the activities transferred, but the factors of production and decision rights often are, too. Factors of production are the resources that make the activities

occur and include people, facilities, equipment, technology and other assets. Decision rights are the responsibilities for making decisions over certain elements of the activities transferred.

There are many reasons to outsource according to previous surveys. Greaver (1999) continues to give some of these reasons and benefits as follows:

Organizationally driven reasons for instance to enhance effectiveness by focusing on what the organization does best, increase flexibility to meet changing business conditions, demand for products and services, and technologies, to transform the organization and to increase product and service value, customer satisfaction, and share-holder value. Improvement-driven reasons are for instance improving operating performance (such as higher quality, increased productivity, shorter cycle times, higher utilization, increased outputs and greater profits), to obtain expertise, skills, and technologies that would not otherwise be available, improving management and control, risk management, to acquire innovative ideas and improve credibility and image by associating with superior providers.

Financially driven reasons include reduction of investments in assets to free up these resources for other purposes and generate cash by transferring assets to the provider. Revenue-driven reasons such as gaining market access and business opportunities through the provider's network, accelerating expansion by tapping into the provider's developed capacity, processes, and systems, expanding sales and production capacity during periods when such expansion could not be financed and commercially exploit the existing skills. Cost-driven reasons such as to reduce costs through superior provider performance and the provider's lower cost structure and turn fixed costs into variable costs. Employee-driven reasons include giving employees a stronger career path and increase the commitment and energy in non-core areas.

2.3.7 Levels of outsourcing

There are three levels of outsourcing namely transformational, tactical and strategic (Brown and Wilson, 2005). Tactical outsourcing is used by organisations to resolve specific problems being experienced by a firm, viz. a lack of financial resources to make capital investments, inadequate in-house managerial competence or a desire to downsize, etc. Tactical outsourcing is a form of

traditional outsourcing and is based on cost comparison and the make-or-buy decision. The tactical outsourcing results in visible benefits in the form of enhanced cash savings, minimising the need for future investments and resolving staffing issues. It involves execution of a business process following the existing rules. Tactical outsourcing can also extend to outsourcing peripheral activities enabling the management to acquire industry specific capabilities by partnering with a chosen vendor (Hussey and Jenster, 2003). This is a common method used by large mature corporations for handling high-volume repetitive tasks. This is used for processes such as payroll transactions, HR administration and procurement.

Strategic outsourcing is used as part of the process of redefining the organisation and results in freeing the management staff to refocus on the core business functions. Strategic outsourcing relationships build long-term value resulting from the client working with a fewer number of best-in-class integrated service providers.

Transformational outsourcing is commonly used to redefine the business (Linder, 2004). It enables an organisation to retain leadership position, build sustainable competitive advantage and generate highest value for an organisation. Some issues addressed by transformational outsourcing are good governance, maturity of business process knowledge and adequately drafted and monitored SLAs. The levels of risk in strategic and transformational outsourcing are higher than tactical form, but are commonly shared with the outsourcing partner. Tested risk mitigation plans, high-security levels, mature project management skills and proven business continuity plans need to be put in place before an arrangement can begin in this direction.

2.4 Research Variables

Evidence presented in Lacity-Hirschheim (1993), Datamonitor (1994), McFarland-Noland (1995), Alexander-Young (1996), O'Heney (1996) and Lacity et al. (1996), among others, supports Williamson's (1975) arguments and suggests reasons below for organizations to outsource some functions. One empirically grounded reason for outsourcing growth was the strategic shift as banks abandoned product and market growth (diversification) strategies to focus on core competencies. Outsourcing also lowers the risks of innovation by turning fixed possibly

uncertain costs into variable costs. In the case of IT based processes like ATMs management many investments failed to deliver the expected competitive advantage. IT expenditure becomes simply a cost of doing business rather than a source of strategic benefit or a source of core competence. The Co-operative Bank through outsourcing, enjoyed access to better quality and more widely experienced staff than they could have attracted into direct employment. Empirical evidence in Lacity et al. (1996) suggests few outsourcers pursue "total outsourcing". The study has three independent variables that is Financial, operational and strategic considerations to outsourcing ATM management and one dependent variable that is organizational performance. The considerations for outsourcing that will be measured under each variable in the conceptual framework are discussed below.

2.4.1 Financial Considerations

Decisions on processing in-house versus outsourcing processing universally consider the costs associated with each option. A comprehensive evaluation of the financial components of the ATM processing decision, however, has three main elements: revenue impacts, expense impacts, and capital requirements.

Generally, the majority of ATM revenues arise from two distinct sources: surcharges and interchange fees from ATM transactions by "foreign" customers (i.e. customers from other financial institutions using the bank's ATMs). Banks also benefit from increased usage of ATMs by their own customers, as well as cross sales of new products to ATM users. Therefore, the bank should consider the effect of the processing decision on foreign transaction volumes, revenue from additional functionality, and revenue from product cross-sales through the ATM channel. Uptime is the single biggest driver of ATM transaction volume. Consistent uptime results from a stable platform, reliable telecommunications, and a closely monitored ATM network. The industry standard for best-in-class ATM availability is 98.5 percent uptime. The potential revenue loss of a network failure during peak hours can significantly influence the profitability of an ATM network. Therefore, processing uptime is an important driver of ATM performance, and a crucial criterion in evaluating processing options. Functionality can also influence ATM network performance. New transaction types, such as additional foreign

languages supported, can increase others-at-us volume. This new volume can benefit the bank through direct transaction revenue or as a reduction in branch servicing costs. In evaluating this element, the bank should consider the internal and external providers' ability to support a given functionality currently, or attempt to estimate differences in time-to-market for functionality not currently supported. Previous studies have encouraged outsourcing of ATM processing if this would translate into increase in revenues and generally the bank's financial performance.

Outsourcing ATM processing converts mostly fixed costs associated with in-house ATM processing to more variable costs, based on the size of the ATM network. Fixed costs are defined as costs that are incurred over the long term (typically more than a year) and do not typically change regardless of the volume of transactions processed. On the other hand, variable costs fluctuate with the volume of transactions (or number of ATMs). An in-house solution can allow the bank to realize lower per unit costs at higher volumes (economies of scale), while outsourced processing allows the bank to avoid high initial investments, and thereby more closely match operating costs with volumes. ATM outsourcing providers benefit from economies of scale in operating their platforms (Plunkett, 2008). These processors spread expenses such as software development, data security, disaster recovery, and network connectivity across many customers' ATMs. That is, processors can spread costs over thousands of ATMs while banks must perform/invest in similar infrastructure to support a dramatically smaller number of ATMs. Economies of scale allow processors to operate at a lower cost structure than all but the largest ATM deployers (Padmalatha, 2011). Therefore, processors can deliver cost savings to banks, and still retain profits. In the outsourcing decision, eliminating redundancies and accessing economies of scale in operations can financially benefit all member banks. Typical expenses, and their respective cost drivers, for maintaining an ATM network in both the in-house and outsourced scenarios include maintenance and servicing costs. A study conducted by NCR in 2001 shows that first and second line maintenance generally cost between \$250 and \$375 per ATM per month. The functions can be performed in-house, or by third parties. Often, banks use a hybrid approach, with in-house resources (e.g., branch staff) performing first line maintenance (paper jams, etc.) and third parties doing second line tasks (i.e., those requiring parts or technical knowledge). Banks must consider costs related to training, transportation, parts inventory, and

human resources for in-house servicing, and monthly cost, response time, and service levels in outsourced environments.

Technology costs such as the hardware and software required to process ATMs represents one of the largest cost drivers. In an in-house environment, they are comprised of purchase or lease expenses for the hardware, and for software, licensing and maintenance fees, or salary and associated costs of in-house developers. In a third party processed environment, the cost of the technology is imbedded in the monthly, quarterly or per transaction charges (NCR, 2006). ATMs require programming to maintain functionality and compliance with network mandates. These changes may include security and functionality upgrades. These technology enhancement costs are shared among other banks if the ATMs are outsourced to the same vendor. Reduction of technology costs translate to improvement in financial performance.

Network Connectivity costs expense category consists of the cost of the telecommunications network and the cost of maintaining interfaces with the network. Economies of scale permit third party processors to negotiate attractive pricing with the telecommunication companies through volume discounts that may not be available to many banks. A bank that maintains a telecom network for its branches may be able to provide connectivity to its branch ATMs at a low cost via shared-use communication lines. Maintaining network interfaces can be expensive and time-consuming. Financial institutions of all sizes, even those that process ATMs in-house, often decide to connect to one processor and allow that party to gateway transactions to all other networks for a per transaction fee.

From time to time, EFT networks require processors (including in-house providers) to support specific functionality requirements such as account-to-account money transfer, ATM deposits, or changes in message format this cost is classified under Network Participation costs. The networks also require processors to make changes to their systems to support evolving operating requirements. Many times system changes require capital investment outside of the "normal" budget cycle and must be made in order to accept foreign transactions. When the bank outsources, third party processors bear the cost of maintaining compliance with network rules. In

other cases, such cost is shared among all of the customers of the processor relieving the bank of the network participation expenses.

ATM back office processing costs include cash management, monitoring and dispatching, ATM balancing and settlement, claims processing, and network settlement. These functions can be performed in-house even if a third party performs the data processing functions. Actual costs are generally a function of the number of ATMs and number of networks used, and somewhat less dependent on transaction volume. In comparing the cost of in-house processing to outsourced processing, or the costs of two potential outsourced providers, banks should consider how these back office costs, which can be significant, will vary. For example, if one provider offers an inferior adjustments system, the bank may require additional staff to perform the adjustments function. The cost of this added staff may exceed any savings associated with the processing services alone. Therefore, a thorough analysis should consider the system functionality in light of back office efficiency.

Kee and Robbins (2003) have utilized Opportunity costs in outsourcing decision models. The outsourcing decision should consider the cost of/return on capital involved. That is, outsourcing can free up capital otherwise invested in ATM processing for other purposes. To evaluate the benefit of this savings, a bank needs to evaluate its other options for capital deployment. Should the bank have other investment options that provide higher returns, such reinvestment opportunities would favor the outsourcing business case.

2.4.2 Operational Considerations

A bank must examine the operational implications of outsourcing its ATM network processing. In this regard, a bank must weigh its current capabilities against any possible improvements and the loss of control associated with outsourcing. While banks have found the promise of additional functionality appealing, many banks have later realized that increased functionality adds only limited value since most customers use the ATMs for deposits and withdrawals only. Nevertheless, ATM deployers realize some value by having additional functionality available (even if not used) since they can more quickly integrate new functions in the future.

Historically, ATMs have allowed customers to check balances and access their bank accounts to transfer or withdraw money. The popularity of additional functions has not driven transaction growth as much as originally expected; however, these upgrades may contribute to the prevention of transaction volume erosion. As such, those networks without advanced features have shown greater decreases in transaction volumes than those networks with more advanced features. Added functionality has driven the cost of transactions much lower than in the past. The elimination of envelopes and the workers required to pickup physical checks both contribute to large reductions in costs for banks. The cost of keeping pace with other banks, however, can be significant. For ATM providers, the desire to keep pace with market improvements requires constant investment. Outsourcing the development and implementation of new features and functions could minimize and “smooth” the investment necessary to keep pace with competition. To minimize the costs of offering new ATM services, banks could consider outsourcing ATM processing. By outsourcing, banks could benefit from participating in a shared platform where the cost of new development is spread across a large customer base. The shared platform also benefits participating banks because the processor performs extensive testing and security audits.

Shared platforms are both stable and highly redundant. Service level agreements (SLAs) inherent in an outsourcing contract assure that the quality of these features and functions will meet banks' expectations. Example service level terms could include uptime of more than 99.5%, while prompt daily reports are delivered 98% of the time. A manager must realize that in order to capitalize on some on-site reliability improvements, it might be necessary to invest in the ATM machines. A bank should take this potential investment into account and its effect on overall operational performance when evaluating the outsourcing decision.

Disaster recovery is an important component of any ATM network to ensure the continuity of business in the event of catastrophic loss. A single bank could face a greater risk of security breach due to less immediate security updates. In the face of a new threat, a bank must develop the security parameter or solution once it is alerted of the issue. Alternatively, a centralized processor typically has the most up-to-date security parameters and dedicated staff to prevent loss of data. By outsourcing processing, a bank increases the security associated with its network

by having backup data available in more than one location. Should a catastrophic loss occur the bank can recover using data backups provided by its processor from a remote location. Additionally, outsourcing processing eliminates the redundancy of multiple recovery systems thereby allowing the cost savings to be passed on to the member banks.

2.4.3 Strategic Consideration

Each bank should carefully consider the decision to outsource, as the ATM is a primary interface with the bank's customers. Outsourcing ATM processing has the potential to not only influence whether customers choose to continue banking with a bank but also whether "foreign" customers choose to use a bank's machines. Managers should consider the implications outsourcing of management of ATMs has on the corporate strategy in the following dimensions:

Competitive differentiation means that while ATM delivery is a critical component of the retail financial services value proposition, it is rare that a bank of any size can achieve and sustain competitive advantage by virtue of its capabilities in ATM processing. That is, banks are unlikely to succeed in the market by virtue of superior ATM processing. While processing ATMs at below market norms can be a negative (i.e., excessive down time), operating ATMs in a manner greater than or equal to market expectations will only allow the bank to achieve competitive parity, not advantage. Therefore, the greater control retained in an in-house environment is unlikely to provide any material strategic advantage however, outsourcing will provide a competitive edge.

Risk Management is another dimension in corporate strategy consideration. By choosing to process transactions internally, a bank incurs various operating risks. These risks include operating failures resulting in service outages, financial losses, customer dissatisfaction or data security breaches along any point in the processing system. Outsourcing transfers this operating risk to the third party processor, but it is replaced with vendor management risk. That is, the bank is at risk in the event of a vendor failure. These risks are normally mitigated by SLAs, and contractual indemnifications from the vendor. The bank must evaluate the relative likelihood of such a failure occurring in both in-house and outsourced scenarios.

Subject Matter Expertise is also a factor under strategic considerations during outsourcing. According to a 2007 research by First Annapolis Consulting regarding Co-op network, if banks support their ATM networks in-house, ATM processing expertise will likely be concentrated among a few key employees. This exposes the bank to the risk that if these employees depart the bank, this expertise leaves with them. Conversely, a small processing staff may be limited in its ability to keep current with industry best practices. By outsourcing the processing function, a bank buys access to greater breadth and depth of expertise.

The bank should also consider the Core Competencies. When evaluating the ATM processing decision, banks should determine if processing ATMs is a core competency. In other words, are the ATM operations centrally important in fulfilling the bank's mission? As such, a bank should focus the majority of managerial time and energy towards this endeavour. If a bank finds itself spending a disproportionate amount of resources on ATM processing, it may benefit from outsourcing processing to a third party.

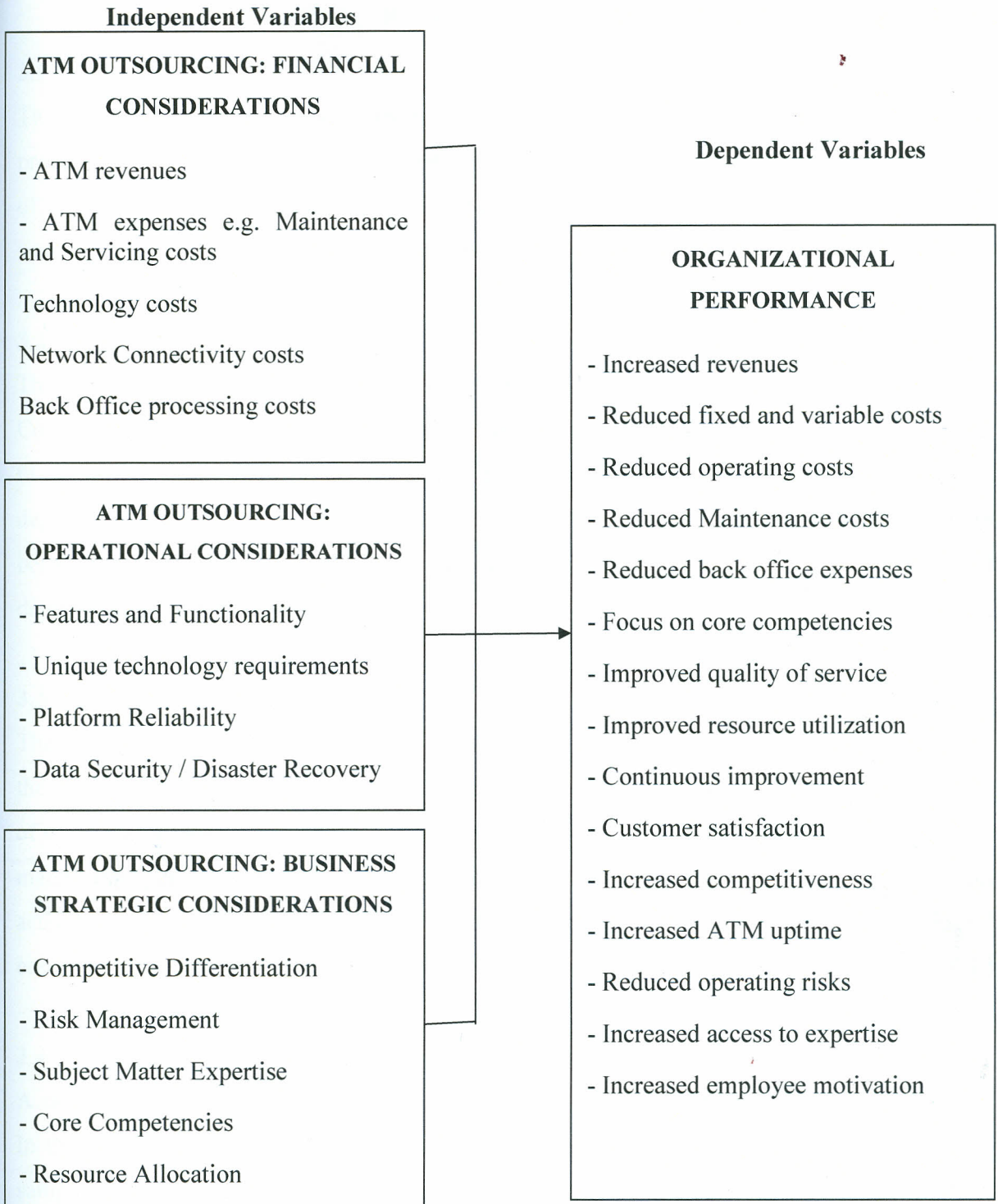
Finally Resource Allocation is also be factored in when making strategic consideration. As previously mentioned, the maintenance and operation of an ATM network is capital intensive. Managers must decide if supporting an in-house ATM network constitutes an efficient allocation of capital. Some managers value the control provided by an in-house solution and are therefore willing to make investments and support the expenses associated with the ATM network. Other managers might consider ATM network operations to be an area of lesser strategic importance and would rather allocate funds to other investments. Similarly, ATM operations require significant management attention to be run effectively. Management could be called upon to deal with issues such as services outages, the implementation of upgrades, machine deployment decisions, and personnel management. By outsourcing, management frees itself to focus on its core business objectives.

2.4.4 Organizational Performance

In this study, the effects of outsourcing on organizational performance was done in more detail by considering the three performance dimensions: financial, operational and strategic. This study is aimed at discovering to what extent Co-op bank revenue increases and how much the ATMs expenses such as operating expenses, maintenance expenses, back office expenses and fixed and variable expenses will reduce if the ATMs are outsourced. The study continued to find out whether there is an increased focus on core competencies, improved resource utilization, reduced customer complaints and improved customer satisfaction when ATMs are outsourced. Other dimensions of performance in relation to outsourcing of ATMs management are for instance improved competitiveness, increased uptime and access to subject expertise and reduced operating risks.

The results presented in this study support or dispute the claims of outsourcing proponents that outsourcing allows organizations to access enhanced expertise, improve service quality, reduce fixed and operating costs, streamline the process, allow focus on core activities and reduce the administrative burden, saving time and increasing revenues. Outsourcing in this sense, is beneficial to organizational performance (Casale, 1996; Crane, 1999; Quinn, 2000). Abraham and Taylor (1996) find that firms “contract out” services with the objectives of smoothing production cycles and benefiting from specialisation. Raa and Wolff (2001) find a positive association between the rate of outsourcing and revenue growth (Jiang and Qureshi, 2006). Elmuti (2003) also provided support for empirical evidence for an outsourcing-productivity relationship. He found that outsourcing accounted for about 40 per cent of the variance in productivity. In summary, firms that outsource any function do so with the idea that the company’s performance will increase (Lilly et al., 2005).

Figure 2.1: Conceptual Framework



Source: Author (2012)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This section describes various methodologies that were used in collecting information, procedures adopted in conducting the research, the techniques used in analysis and presentation of data collected. This chapter therefore focused on the study design, population, population sample, sample design and data collection and analysis applied during the study.

3.2 Study Design

This study used a descriptive design. It enabled an in-depth understanding of the phenomena. Consequently, the study focused on specific Co-operative bank departments directly or indirectly involved with the decision to outsource the management of the bank's ATMs and the departments directly or indirectly affected by the outsourcing decision. The design is preferred because of proximity of the case and faster access to information. More important it permits in-depth scrutiny of phenomena at hand.

3.3 Target Population

The unit of analysis in this study was Co-operative bank. The population of study comprised of the various profit centres contributing to performance i.e. the bank's branches. The population of study was all the 39 branches in Nairobi region. Out of each branch, the study targeted branch managers, operations managers and team leaders as the key respondents as they have been actively involved in the outsourcing process. Nairobi Area is subdivided into five regions for ease of management. The size of potential respondents under each region are shown in table 3.1.

3.4 Sampling Design and Sample Size

A sample is a representative proportion of a population selected from observation and analysis. In this study, the researcher used cluster and stratified random sampling technique to select a sample of 55 respondents. The cluster was the geographical region in Nairobi area; the strata was be management levels i.e. top management, middle management and team leaders or branch assistants. From the research, a sample was selected using proportional simple random sampling.

	Region	Number of Branches	Top Level Managers (Pop. Size)	Top Level Managers (Sample Size)	Middle level Managers (Pop. Size)	Middle level Managers (Sample Size)	Team leaders/ Branch assistants (Pop. size)	Team leaders/ Branch assistants (Sample size)	Total sample size
1	Nairobi Central	17	17	7	17	8	17	9	24
2	Nairobi North	5	5	2	5	2	5	3	7
3	Nairobi East	7	7	3	7	3	7	4	10
4	Nairobi South	6	6	2	6	3	6	3	8
5	Nairobi West	4	4	2	4	2	4	2	6
	Total	39		16		18		21	55

Table 3.1 Sample Size (Author, 2012)

Key:

Pop. – Population

3.5 Data Collection Instruments and Procedures

In order to collect data comprehensive data, the researcher used questionnaire. The method considered was ideal this being a qualitative study. The respondents to the questionnaire were key persons in various branches at Co-operative Bank Nairobi region who have an in-depth understanding and fully conversant with the outsourcing decisions at the bank. The purpose of the research questionnaire was to gather information on the outsourcing implications. The questionnaire was designed to elicit meaningful answers. First primary data was collected using questionnaire and this is the main data to be used in research. The questionnaire was administered by email and was not be pre-tested. Pre-developed questionnaire needed for pre-testing was not financially feasible for carrying out this research project. Secondary data involved collection of already processed information through a literature review sourced from libraries, internet and journals.

3.6 Data Analysis and Presentation Methods

The data collected was analyzed by use of descriptive statistics. Descriptive statistics used was mean and standard deviation while correlation analysis was used to assess the nature of relationship between the independent and dependent variables. In particular, frequency tables, averages and percentages was used. The data was then presented using tables, graphs and charts.

3.7 Expected Output

Reference to the objectives and analysis to be conducted it was possible to realize the purpose of this study. An assessment of the effect of ATM outsourcing decisions on the performance of Co-operative bank was done using the discussed research tools. The researcher also drew conclusions based on the field findings.

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION

4.1 Introduction

Thirty-four (34) respondents took part in the study: male (55.9%) and female (44.1%). The majority of the respondents (41.2%) had worked for cooperative bank for about three to five years (3-5 years) compared to those who had worked for less than one year (11.8%) and over ten years (14.7%).

Table 4.1: Gender of respondents

	Frequency	Percentage	Valid Percent
Male	19	55.9	55.9
Female	15	44.1	44.1
Total	34	100.0	100.0

Table 4.2: Number of Service years with Coop Bank

	Frequency	Percent	Valid Percent
Less than one year	4	11.8	11.8
1 -2 Years	4	11.8	11.8
3 - 5 Years	14	41.2	41.2
6 - 10 Years	7	20.6	20.6
10+ years	5	14.7	14.7
Total	34	100.0	100.0

Individuals working for Cooperative Bank show some enticing commitment and dedication to their work as it is clear from these results. These is due to the fact that the bank has plans and strategies of retaining workers for long in order to unleash all their potentials and skills for the

betterment of the company performance. It shows that the company has the ability of keeping members for most of their productive ages before members opt for other careers outside the bank. The bulk of workers at the bank are those who have worked for 3-5⁺ years and their percentage stand at 41.2%. This is a good percentage for working period for most of the focused organizations, since it is, a time they can achieve more from their employees and training they have gone through find maximum utility. During this period, workers still want to proof that they can produce outstanding results, after which they can now be hired by other organizations or move to private sectors after they have stabilize. This group represent a large percentage of those who have just finished their studies and this may be their first jobs. On the other hand, those who have worked for the bank for more than 6-10 years are second with a percentage of 20.6%. This indicates some sense of commitment and work satisfaction. This group proves that the bank offers the best working conditions and workers should be ready at all times to serve the organization as it protects their interests at the expense of the services offered. The 20.6% is a surety that the bank offers internal training to keep workers for long and ensure continued performance. The third group are those who have been in the company for over ten years. A 14.7% for long serving employees means the bank's performance is guaranteed where it works to ensure job security of all employees. These workers have matured in management, as they know every aspect of the bank. The bank depends on them for major decisions and directions as they have a pool of experiences. The other ratio consists of occasional workers who have just been introduced to the bank. This group is important as they have new skills and ideas from other areas within the sector or colleges and their support is highly encouraged. The group at 11.8% balances those who are almost retiring or have moved to other sectors and careers. The group consist of both new job seekers and those with experience hence a perfect coordination as they teach one another on how performance may be achieved uniformly.

Table 4.3: Number of years ATM services outsourced at the Coop branch

	Frequency	Percent	Valid Percent
0 Years	1	2.9	2.9
0 - 2 Years	9	26.5	26.5
2 - 5 Years	17	50.0	50.0
6 - 10 Years	7	20.6	20.6
Total	34	100.0	100.0

The cooperative bank for quite some time has been outsourcing their ATM service to recognized vendors. For some reasons the bank have outsourcing part of the services in order to reduce risks and seek other alternative that may work best for the company outsourcing services. For instance, the bank outsourced 50.0% of ATMs between 2-5 years to ensure they have some control over the other half in case risks arise they can use those to protect the client loyalty. The bank also has outsourced a number of other ATMs for between 6-10 years and the percentage stands at 20.6%. This percentage is due to some past successes and bank's performance due to the outsourcing. The percentage indicates that the bank has benefited from outsourcing since the percentage is relatively high. The world is now changing and every aspect is moving to technological inventions hence, the company have chosen to outsource for longer periods in order to work on internal management as the external needs more time and adjustments that they may not be in position to handle both. Currently, the banking sector is moving global where money is being moved from one country to another in form or e-cash. Such factors can be difficult for the bank to manage and still ensure performance of its operations as they require additional evaluation efforts that may be costly for them. For that, they have chosen to outsource ATMs service for longer period so that any changes or new conditions about ATMs operation performance and e-banking may be handled smoothly and keep the company at its level best at all times.

4.2 The extent to which the statements are true regarding effects of ATM management outsourcing on financial performance of the cooperative bank of Kenya

Although 1% of the respondents do not support the claim that ATM management outsourcing has reduced back office processing and maintenance. A majority of respondents at 47.1% to high extent agree that ATM management has reduced outsourcing back office processing and maintenance; technology improvements costs, and high fixed costs to variable costs when ATMs are outsourced.

This is followed by very high extent at 29.4% and those who said to a moderate extent at 20.6%. Thus, ATM management outsourcing reduces back office processing and maintenance, technology improvements costs, and high fixed costs to variable costs contributing to the financial performance of the Cooperative Bank of Kenya.

It is understandable if ATM operators feel like they are caught between the proverbial rock and a hard place. While a stream of regulatory changes and technological upgrades batters the bottom line, market forces lead to lower transaction volumes and reduced fee income.

To combat these forces, Cooperative Bank has turned to new functionalities, such as mobile banking, automated deposits and billpay, to attract new customers and retain existing customers and members. However, that leads to greater complexity and management challenges in integrating branch, mobile, and ATM channels for a seamless customer experience.

Financial institutions today are exploring more outsourcing opportunities to have a skilled ATM services provider handle some of the more time-consuming ATM procedures, such as transaction processing, remote management, cash optimization, service and regulatory compliance.

Table 4.4: Extent ATM outsourcing has reduced back office processing and maintenance

	Frequency	Percent	Valid Percent
Very High Extent	10	29.4	29.4
High Extent	16	47.1	47.1
Moderate Extent	7	20.6	20.6
Not at All	1	2.9	2.9
Total	34	100.0	100.0

The dedicated ATM management program provides Cooperative Bank with total control and visibility into the cost, status, and reliability of their ATM network, removing the burden of network operation so they can focus on the initiatives that will deliver the greatest impact for the bank. With a customized outsourced ATM management solution, the bank will improve the performance of their network while providing advanced functionality support often months or years before they otherwise could. They enjoy improved ATM uptime, reduced management overhead, and so much more. There is a very high extent of 29.4% that ATM outsourcing lowers back office processing and maintenance due to following benefits:

- Single-source solution: One source for all your ATM management needs – ATMs specialists provides best in class services through a combination of company-owned resources and handpicked partners.
- Multi-platform support: Outsourced vendor works with every major ATM manufacturer and supports a wide range of software, hardware, communication, and other parameters. No need for multiple vendors to support multiple manufacturers or models.
- Dedicated relationship manager: A single point of contact is only a phone call or e-mail away, standing by to handle any problems that might arise and proactively helping to maximize the value of bank’s ATM program for them as well as their customers.
- Online dashboard: Complete visibility into network performance 24/7/365 through a dedicated, secure online dashboard providing at-a-glance information from the network

level down to the individual ATM is available for outsourcing.

- Single-page invoice: Easy-to-understand billing with 100% clarity into the cost of service.
- Marketing and customization programs: Market directly to bank's customers through targeted advertising campaigns and true one-to-one marketing initiatives. Stored preferences allow bank's customers to customize their ATM experience.
- Direct processing connection: Using the in-house processing platform, outsourced firms can connect directly to your networks for improved performance and uptime as well as advanced functionality support.

Table 4.5: Extent ATM outsourcing has reduced technology improvements costs

	Frequency	Percent	Valid Percent
Very High extent	10	29.4	29.4
High Extent	16	47.1	47.1
Moderate extent	7	20.6	20.6
Not at all	1	2.9	2.9
Total	34	100.0	100.0

With every outsourcing solution, no matter how large or small, the bank ensures that its customers are receiving the best ATM experience while the staff are relieved of the operating and financial burdens typically associated with a bank-owned ATM program. The bank can now focus on what matters most to their business, as they trust ATM management to outsourcing firms. It was initially regarded as a standardised service, but it has become more of a differentiable offering in recent years due to developments in ATM technology. As the technology evolves and becomes more sophisticated, outsourcing typically gives banks greater access to the latest technologies and innovations, enhancing the service they can provide their customers. However, perhaps the biggest advantage of ATM outsourcing for Cooperative bank in the present environment is cost efficiencies. At the current time, lowering overheads is high on

the industry's agenda and outsourcing ATM estates can contribute to this drive for cost reduction.

Table 4.6: Extent the bank has reduced high fixed costs to variable costs,

	Frequency	Percent	Valid Percent
Very high extent	8	23.5	23.5
High extent	15	44.1	44.1
Moderate extent	10	29.4	29.4
Not at all	1	2.9	2.9
Total	34	100.0	100.0

To a high extent (38.2%), costs are spread over a large number of ATMs when ATM management is outsourced. This is followed by very high extent at 29.4%, moderate extent at 26.5% and those who either said little extent of not at all at 2.9%. This therefore implies that with ATM management outsourcing, costs are spread over a large number of the ATMs contributing in one way or another to the financial performance of the bank.

Among the top motivators are cutting time to maintain the ATM estate, reducing operational costs, focusing more on core business activities, and staying up to date with current technology. For Cooperative bank, managing an estate of ATMs across the Kenya requires management of numerous separate contract relationships to deliver this end-to-end service but for the banks' internal resources, the management of these contracts and relationships is a time-intensive task.

However, the full-service outsourcing of ATMs delivers the efficiency of providing one single point of accountability, under a single contract, which is much easier to manage for the bank and allows them to take advantage of the economies of scale provided by a specialist organisation.

By handing over the management of the estate to an industry specialist, valuable internal resources can be freed-up as bank is able to take advantage of expertise they would not find in-house. Cooperative Bank of Kenya can then use these resources to deliver services that support the bank's core business objectives.

Table 4.7: Extent costs are spread over a large number of ATMs

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	13	38.2	38.2
Moderate extent	9	26.5	26.5
Little extent	1	2.9	2.9
No at all	1	2.9	2.9
Total	34	100.0	100.0

The study also revealed that to a high extent (52.9%) because of ATM management outsourcing, economies of scale allow third party processors to negotiate attractive pricing through volume discounts that may not be available to the bank. Those who said follow this to a moderate extent at 26.5%, very high extent at 17.6%, then little extent and not at all at 5.9% and 2.9% respectively; therefore, contributing to financial performance of the cooperative bank.

Outsourcing to a trusted service provider eliminates these time-consuming tasks and allows for greater focus on core competencies, including customer acquisition and retention. In addition, not only does ATM outsourcing allow the bank to free up internal resources to focus on more business-critical areas, but it also provides the financial institution with access to a much wider pool of experience and dedicated ATM expertise. The levels of expertise required to outsource ATM services successfully are sometimes not available in-house and it is exactly this type of expertise, which is crucial to keeping the performance running effectively and efficiently 24 hours a day.

Table 4.8: Extent economies of scale allow attractive pricing

	Frequency	Percent	Valid Percent
Very high extent	6	17.6	17.6
High extent	18	52.9	52.9
Moderate extent	7	20.6	20.6
Little extent	2	5.9	5.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

To a high extent (35.3%), ATM management outsourcing leads to increased opportunity cost of capital i.e. free up capital for other important projects. Those who feel that to a very high extent (32.4%) follow this closely and those who do not agree at all stand at 2.9%. This result reveals therefore that ATM management outsourcing leads to increased opportunity cost of capital thus contributing to financial performance of the bank in a way.

Indeed, the management of estates is becoming increasingly complex with transaction processing, cash management and software upgrades all requiring continual review. For cooperative bank with limited expertise in this area, ATM outsourcing can prove particularly attractive as it goes beyond the simple purchase, renting and maintenance of hardware and can incorporate installation, transaction processing, cash handling, communication, cleaning, maintenance and remote monitoring. The bank may also adopt as much or as little of this service as they require, from outsourcing the whole ATM network, to only outsourcing specific elements – for example, the real-time monitoring of the network to maximise up time.

Table 4.9: Extent of increased opportunity cost of capital

	Frequency	Percent	Valid Percent
Very high extent	11	32.4	32.4
High extent	12	35.3	35.3
Moderate extent	7	20.6	20.6
Little extent	3	8.8	8.8
Not at all	1	2.9	2.9
Total	34	100.0	100.0

When it comes to the extent to which network participation expenses are shared with several other banks outsourcing ATMs to the same provider, the majority of the respondents said to high extent at 52.9%, followed by those who said to very high extent at 20.6% and those who do not support the statement at 8.8%. Thus network participation expenses are shared with several other banks outsourcing ATMs to the same provider affecting the financial performance of the bank.

Aside from the obvious benefits the bank may get from Outsourcing, the full-service outsourcing option is particularly compelling for small to medium-sized banks who may be struggling to justify the need to invest continually in technology, compliance, and physical ATM replacement. Cooperative bank have to monitor the performance of each ATM in the network to ensure that it continues to support customer needs. ATM placement must be regularly reviewed to confirm that each ATM is continuing to operate at peak performance, thereby optimising the costs of operation. This represents an obvious drain on resources for the smaller-sized bank. In addition, if cooperative bank neglects to invest in their ATM machines, they will face an ageing estate that is costly to maintain and increasingly unreliable.

Outsourcing the management of the ATM estate provide a cost-effective opportunity for a wholesale technology refresh without the need for capital investment. Keeping the ATM estate current goes beyond simply updating hardware. For instance, outsourced providers can effect change quickly and share the costs of any changes across a broader base of users. These costs

could cover innovation within the ATM transaction set but also the costs of scheme compliance. As a result, the bank can focus on making strategic decisions around its ATM estate and customer proposition.

Outsourcing in some cases may also be the only feasible option if a sizable capital investment is required. In these instances, the bank should carefully analyse the total cost of ownership associated with the overall management of ATMs, and benchmark it against vendors' rates for outsourcing services, and, if possible, against peers. For industry growth and customer reliability, banks also need to ensure that their supplier understands the regulatory requirements that are growing around outsourced services.

Table 4.10: Extent to which network participation expenses are shared

	Frequency	Percent	Valid Percent
Very High extent	7	20.6	20.6
High extent	18	52.9	52.9
Moderate extent	5	14.7	14.7
Little extent	3	8.8	8.8
Not at all	1	2.9	2.9
Total	34	100.0	100.0

Outsourced suppliers are particularly beneficial to the bank, as they often have a better insight into the performance of the national ATM network as well as more advanced tools at their disposal to help select locations for ATMs based upon a bank's customer portfolio. This approach supports the bank in creating more customer 'loyalty' in their selection and usage of ATMs and can reduce levels of interchange. It is clear that ATM outsourcing not only creates savings but it also aids development. In a recession, it is crucial for banks to ensure they retain and potentially acquire new customers. During a time when internal spend is low, however, outsourcing is often the only way to develop new products for the bank – freeing up resources within the bank to focus on providing a greater customer service and also providing access to expertise not currently available within the company.

4.4 The extent to which the statements are true regarding contributions of ATM management outsourcing on operational considerations of the cooperative bank of Kenya

The table below reveals that to high extent (47.1%) ATM management outsourcing increases uptime and reliability of ATMs, compared to those who either agree to a little extent and those who said not at all at 2.9%. Thus, ATM management outsourcing contributes to operational considerations at the cooperative bank because it increases uptime and reliability of ATMs. Despite the challenges, ATM management poses to banks, ATM networks have proven to facilitate in attracting new customers and promote self-service banking and convenience.

Table 4.11: Extent ATM outsourcing increase uptime and reliability of ATMs

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	16	47.1	47.1
Moderate extent	6	17.6	17.6
Little extent	1	2.9	2.9
No at all	1	2.9	2.9
Total	34	100.0	100.0

For these reasons, cooperative bank will always need to deploy off-premises ATMs as part of their branding and service efforts. The decreasing profitability of bank-owned and operated ATMs has made full-service ATM outsourcing an ideal means to achieve the balance between revenue and visibility. With such a complex landscape, the case for outsourcing ATM estates, and tapping into an existing knowledge pool, is a strong one.

ATMs automated the issuing of cash several decades ago and now self-service banking is moving into the next phase with deposit and cash recycling machines in the market. All of these new devices need the same care and support as the ATM, meaning reliability, and availability are of paramount importance. As the ‘face’ of the bank for the customer, cooperative bank must

provide the best service possible by ensuring ATM fleets are fully functioning as well as compliant with changing regulatory, technology, and customer needs.

Table 4.12: Extent ATM outsourcing allows bank to leverage new technologies

	Frequency	Percent	Valid Percent
Very High extent	9	26.5	26.5
High extent	17	50.0	50.0
Moderate extent	7	20.6	20.6
Not at all	1	2.9	2.9
Total	34	100.0	100.0

There are risks in outsourcing, but today, more than ever, there is leverage to ensure third party providers are committed. The services offered by a vendor are their core competency functions. Superior third party providers understand that success means meeting the needs of their customers by concentrating on their core functions. In the table above, the data revealed that to a high extent (50%) ATM management outsourcing allows cooperative bank to leverage new technologies to improve customer service, contributing to operational considerations of the bank. However, 2.9% of the study does not support the statement, whereas 26.5% and 20.6% agree to a very high extent and moderate extent respectively.

Table 4.13: Extent outsourcing enables adaptation of customized operating platform

	Frequency	Percent	Valid Percent
Very High extent	11	32.4	32.4
High extent	14	41.2	41.2
Moderate extent	6	17.6	17.6
Little extent	2	5.9	5.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

When it comes to extent ATM management outsourcing enables adaptation of customised operating platform, the study revealed a high extent of 41.2% followed by very high extent at 32.4%, moderate extent 17.6%, little extent and not at all at 5.95 and 2.9% respectively. Thus, to a high extent ATM management outsourcing enables adaptation of customised operating platform; contributing to operational considerations of the bank.

Table 4.14: Outsourcing increases access to greater breadth and depth ATM management

	Frequency	Percent	Valid Percent
Very High extent	10	29.4	29.4
High extent	12	35.3	35.3
Moderate extent	11	32.4	32.4
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The study was also to determine the extent to which ATM management outsourcing increases access to greater breadth and depth of ATM management expertise. The table above shows that a minor majority of respondents agree to the statement at a high extent (35.3%). This is followed by those who agree to moderate extent (32.4%), very high extent (29.4%) and not at all (2.9%) in that order. This therefore implies that ATM management outsourcing increases access to greater breadth and depth of ATM management expertise contributing to operational considerations.

Table 4.15: Outsourcing eases data back up and access to better recovery system

	Frequency	Percent	Valid Percent
Very high extent	6	17.6	17.6
High extent	17	50.0	50.0
Moderate extent	9	26.5	26.5
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The study also revealed that ATM management outsourcing eases data backup and access to better recovery systems leading to operational considerations in the bank. This is evident from the above table where the majority of the respondents agree with the statement to a high extent at 50%, moderate extent at 26.5%, very high extent at 17.6%, little extent and not at all at 2.9%.

Table 4.16: Outsourcing eliminates redundancy of multiple recovery systems

	Frequency	Percent	Valid Percent
Very high extent	9	26.5	26.5
High extent	16	47.1	47.1
Moderate extent	6	17.6	17.6
Little extent	2	5.9	5.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The study was also thought to confirm the extent ATM management outsourcing eliminates redundancy of multiple recovery systems when it comes to operational considerations in the bank. It is thus clear from the table above that the majority of the respondents support the statement to a high extent (47.1%) compared to those who do not support at all (2.9%). Implying

that ATM management outsourcing eliminates redundancy of multiple recovery systems and is therefore forms part of the operational considerations of the bank.

Table 4.17: Outsourcing has led to increase in number of new services provided to customers

	Frequency	Percent	Valid Percent
Very high extent	7	20.6	20.6
High extent	18	52.9	52.9
Moderate extent	6	17.6	17.6
Little extent	2	5.9	5.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

Another concern relating to the operational consideration of the bank was the extent to which ATM management outsourcing has led to the increase in the number of new services provided to customers within the bank. The study revealed that 55.9% agree to a high extent followed by 10% agreeing to very high extent and to moderate extent at 8.8% while little extent and those who did not agree at all at 2.9%. Thus ATM management outsourcing when it comes to number of new services provided to customers forms part of the operational considerations of the bank.

4.3 The extent to which the statements have made contributions regarding strategic considerations of the bank regarding ATM management outsourcing

The study was to determine the extent to which outsourcing has led to focus on core competencies. The table below shows that to a high extent (55.9%) agree with the statement compared to 2.9% who either say to a little extent or not at all. This means that ATM management outsourcing to a high extent contribute to strategic considerations of the bank when it comes to core competencies.

Table 4.18: Extent outsourcing has led to focus on core competencies

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	19	55.9	55.9
Moderate extent	3	8.8	8.8
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The research was also to find the extent to which ATM management outsourcing has led to increase in levels of utilization of resources increase i.e. in-house staff. The result agree with the statement as the majority either said to very high extent of high extent at 35.3% followed by moderate extent at 26.5% compared to those who said not at all at 2.9%. Implying that with ATM management outsourcing, there will always be increase in in levels of utilization of resources forcing the bank to take some strategic considerations.

Table 4.19: Outsourcing has led to increase in levels of utilization of resources

	Frequency	Percent	Valid Percent
Very High extent	12	35.3	35.3
High extent	12	35.3	35.3
Moderate extent	9	26.5	26.5
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The table below shows that to a high extent (52.9%), ATM management outsourcing has led to reduction of customer complains. However, 29.4% agree with the statement to a very high extent

compared to moderate and not at all at 14.7% and 2.9% respectively. This therefore implies that the high extent compels the bank to take strategic considerations.

Table 4.20: Outsourcing has led to reduction of customer complaints

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	18	52.9	52.9
Moderate extent	5	14.7	14.7
Not at all	1	2.9	2.9
Total	34	100.0	100.0

On concerns about quality of service delivery, the results reveal the minor majority of respondents agree with the statement to a high extent (38.2%). This is followed closely by those who agree with the statement to a moderate extent at 32.4, then very high extent at 26.5% and not at all (2.9%). Thus, ATM management outsourcing has to high extent led to reduced concerns about quality of service delivery, compelling the bank to take strategic considerations.

Table 4.21: Outsourcing has reduced concerns about quality of service delivery

	Frequency	Percent	Valid Percent
Very high extent	9	26.5	26.5
High extent	13	38.2	38.2
Moderate extent	11	32.4	32.4
Not at all	1	2.9	2.9
Total	34	100.0	100.0

Although the results reveal that 2.9% do not agree with the statement at all, 44.1% agree to a high extent (44.1%). This therefore implies that ATM management outsourcing has increased competitiveness, requiring the bank to take strategic consideration.

Table 4.22: Extent outsourcing of ATM has increased competitiveness

	Frequency	Percent	Valid Percent
Very High extent	12	35.3	35.3
High extent	15	44.1	44.1
Moderate extent	6	17.6	17.6
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The tables 4.4 and 4.5 below also show that ATM management outsourcing has led to continuous improvement and reduces operating risks to a high extent (41.2%). Those who support this statement to a very high extent at 29.4%, then moderate extent at 23.5% closely follow this. However, 2.9% agree either to a little extent or not at all. Thus, ATM management outsourcing has led to continuous improvement and reduction in operating risks to a high extent and thus forcing the bank to always take a strategic consideration.

Table 4.23: Extent outsourcing ATM has led to continuous improvement

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	14	41.2	41.2
Moderate extent	8	23.5	23.5
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

Table 4.24: Extent outsourcing ATM reduces operating risks

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	14	41.2	41.2
Moderate extent	8	23.5	23.5
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The study also showed that ATM management outsourcing improves quality of services of the bank with a majority either saying to high extent or to a moderate extent at 35.3%. However, 2.9% disagreed to a little extent or not at all. Thus, ATM management outsourcing improves quality of services requiring the bank to include it in its strategic considerations.

Table 4.25: Outsourcing of ATM improves quality of service

	Frequency	Percent	Valid Percent
Very high extent	8	23.5	23.5
High extent	12	35.3	35.3
Moderate extent	12	35.3	35.3
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

4.5 The extent statements are true regarding performance of Cooperative Bank in relation to outsourcing of ATM management.

Compared to 2.9% either who agree to a little extent or not at all, tables 1&2 show that to a high extent (44.1%) ATM management outsourcing has led to reduction of costs and increase in revenue at the cooperative. Thus, ATM management outsourcing contributes to the general performance of the cooperative bank to a high extent. This study concurs with Gilley and Rasheed (2000) who proposed that organizational performance in financial institutions improves for three reasons. First, an increased focus on a firm's core competencies is an important benefit associated with outsourcing (Dess *et al.*, 1995; Gilley and Rasheed, 2000; Kotabe and Murray, 1990; Venkatraman, 1997).

Table 4.26: Extent outsourcing has led to reduction of costs

	Frequency	Percent	Valid Percent
Very high extent	9	26.5	26.5
High extent	15	44.1	44.1
moderate extent	8	23.5	23.5
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

Table 4.27: Extent ATM outsourcing has increased revenue

	Frequency	Percent	Valid Percent
Very high extent	9	26.5	26.5
high extent	15	44.1	44.1
Moderate extent	8	23.5	23.5
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

When it comes to the extent to which ATM management outsourcing has increased productivity levels, the results reveal that to very high extent at 38.2% followed by moderate extent at 35.3%. While high extent and not at all at 23.5% and 2.9% respectively. This implies that ATM management outsourcing has increased productivity levels leading to increased general performance of the bank.

Table 4.28: Extent ATM outsourcing has increased productivity levels

	Frequency	Percent	Valid Percent
Very high extent	13	38.2	38.2
High extent	8	23.5	23.5
Moderate extent	12	35.3	35.3
Not at all	1	2.9	2.9
Total	34	100.0	100.0

The study also looked at the extent ATM management outsourcing has boosted employee motivation levels. Employee motivation is motivated to a high extent (44.1%); thus improving the general performance of the bank.

Table 4.29: Outsourcing ATM has boosted employee motivation levels

	Frequency	Percent	Valid Percent
Very high extent	10	29.4	29.4
High extent	15	44.1	44.1
Moderate extent	6	17.6	17.6
Little extent	2	5.9	5.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

When it came to the extent ATM management outsourcing has ensured repeat customers, the results reveal that to very high extent (41.2%) agree with the statement as they believe that this leads to performance of the bank.

Table 4.30: Outsourcing ATM has ensured repeat customers

	Frequency	Percent	Valid Percent
Very high extent	14	41.2	41.2
High extent	11	32.4	32.4
Moderate extent	6	17.6	17.6
Little extent	2	5.9	5.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

In the table below, the study shows that ATM management outsourcing has provided the bank a competitive edge to a high extent (38.2%). However, 2.9% either agree to a little extent or do not agree at all. Thus, to a high extent ATM management outsourcing affects the general performance of the bank.

Table 4.31: Outsourcing ATM has provided the bank a competitive edge.

	Frequency	Percent	Valid Percent
Very high extent	11	32.4	32.4
High extent	13	38.2	38.2
Moderate extent	8	23.5	23.5
Little extent	1	2.9	2.9
Not at all	1	2.9	2.9
Total	34	100.0	100.0

4.6 Discussion

From this study, outsourcing ATMs at coop bank will most likely increase and the bank will concentrate more on the core competencies while assigning ATMs maintenance activities to vendors. Although the move toward outsourcing is increasing among banks, the effect of this application on the organizational performance is not fully known. There are many theoretical studies on the positive effects of outsourcing (Lilly et al., 2005; Perry, 1997; Quinn, 1999). However, the number of empirical studies analysing these theoretical approaches is very limited (Jiang and Qureshi, 2006; Mahnke et al., 2005). While technological advances offer new potential sources of revenue for the bank, investment requirements to keep up with industry developments can be daunting. In light of the new business realities, the old arguments against outsourcing have been turned upside down. Outsourcing is growing in popularity as more organizations conclude that the risks of outsourcing non-core functions are losing their relevance and may not be valid in today's harsh economic environment. This paper describes why Cooperative Bank of Kenya has renewed and intensified interest in outsourcing to cut costs quickly, avoid new capital investment, remove assets from the balance sheet, and address ever-increasing regulatory reporting and compliance burdens.

The findings in this study is in agreement with previous studies which found that outsourcing reduced costs (Jiang *et al.*, 2006; Prater, 1999; Smith *et al.*, 1998), increased productivity (Elmuti, 2003), profitability (Espino-Rodríguez and Padrón-Robaina, 2005) and quality (Elmuti, 2003; Espino-Rodríguez and Gil-Padilla, 2005) and overall improve organizational performance. The results of this study support previous research findings by Lilly et al. (2005) and Perry (1997) that the strategic, financial and operational factors need to be considered and how they will influence the decision to outsource. Based on survey data, the results of this paper indicate that cooperation with a vendor has led to significant improvement in effectiveness, productivity, profitability, quality and continuous improvement. Bank managers in this study feel that organizational performance has increased after outsourcing.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

While ATM delivery is a critical component of the retail financial services value proposition, it is rare that a financial institution of any size can achieve and sustain competitive advantage by virtue of its capabilities in ATM processing. That is, banks are unlikely to succeed in the market by virtue of superior ATM processing. Note that this statement is not in conflict with the premise that number, location, and availability of ATMs can be a differentiator. Rather, while processing ATMs at below market norms can be a negative (i.e., excessive down time), operating ATMs in a manner greater than or equal to market expectations only allow banks to achieve competitive parity, not advantage. Therefore, the greater control retained in an in-house environment is unlikely to provide any material strategic advantage. More importantly, Cooperative bank must evaluate the relative likelihood failure occurring in both in-house and outsourced scenarios. For example, a third party processor may provide a more secure network than a typical financial institution can develop internally, which reduces the chances of a data breach.

5.2 Conclusions

The results from this study provide evidence to support the argument that there is a positive relationship between outsourcing and organizational performance through cost savings, streamlining operations and achieving a competitive advantage. For each of the financial, operational, and strategic factors identified, the bank evaluates the distinct advantages and disadvantages on a case-by-case basis. There is no simple answer as to whether or not the bank should outsource its ATM network. Instead, the management objectively and individually evaluate the merits of in-house versus outsourcing options to select the best solution for the bank. This research shows that while operational demands for servicing and maintaining ATMs increase, the bank tends towards outsourcing ATM management to a third party. Operational considerations include the need to ensure platform reliability and implement data security

measures. Experiencing extended platform downtime or a security breach could have a profoundly negative impact on member relations. Given the importance of these items, the bank must weigh its current capabilities against any possible improvements and the loss of control associated with outsourcing. The relationship between performance and outsourcing also varied with differing levels of operational considerations. In branches, where ATMs custodians were involved in all aspects of ATM management from cash replenishment to clearing of minor errors the performance was positively related to the outsourcing process when these tasks were turned over to the outsourced company. One reason for this finding maybe the time associated with monitoring and maintaining the ATM increase in more dynamic environments. In addition, rapidly changing technologies may allow supplier firms, which specialize in developing and/or implementing a particular technology or process are able to do so without impacting their firms whilst if the technology was to be developed by the banking institution it will mean dedication of more manpower and finances.

The findings of this study also showed the bank is aggressively pursuing cost/financial leadership strategies to gain more on outsourcing of ATMs management. There is a positive relationship between outsourcing and financial considerations the bank make by weighing the expenses against the profits generated when ATMs are outsourced. The major expense categories associated with supporting an ATM network for cooperative bank are maintenance and servicing, technology support, network connectivity, network participation, back office functions, and opportunity cost of capital. Processing almost universally benefits from increased scale, meaning the incremental costs of processing transactions decreases as larger volumes are processed on the same platform. Specialist processors achieve significant economies of scale benefits by consolidating the resources necessary to process ATM transactions. These benefits often allow processors to offer the above listed services at a cost below what a bank could achieve in-house. Back office costs are the exception in that many functions can be performed in-house even if a third party performs the data processing functions. Actual back office costs are generally a function of the number of ATMs and numbers of networks used, and are less dependent on transaction volume.

Finally, this research showed that Cooperative Bank has gained from outsourcing ATMs by allowing the bank's management to focus and allocate resources towards core competencies. Strategic issues take into account the effect on the bank's performance and competitive positioning based on the processing capabilities and service levels observed. Specific strategic considerations for Cooperative bank include competitive differentiation; focus on core competencies, resource allocation, risk management, and subject matter expertise. While ATM delivery is a critical component of the retail financial services value proposition, it is rare that a financial institution of any size can achieve and sustain competitive advantage by virtue of its capabilities in internal processing.

5.3 Recommendations

In connection with the findings of the study and discussions and conclusions, some recommendations can be made for banks and other financial institutions. This does not mean that all banks will benefit from outsourcing. For this reason, it is crucial that the senior management make a cost-benefit analysis after obtaining all the information necessary on outsourcing. The pros and cons of outsourcing should be evaluated properly. Although outsourcing has its benefits, it also bears risks for banking institutions. This study shows that by outsourcing, management frees itself to focus on its core business objectives thereby improving performance. In cases where the financial rationale for outsourcing is ambiguous, the most often cited reason to outsource is the desire to save management time and eliminate these "hidden" costs.

The greatest limitation of this study was that the impact of outsourcing on a company's performance relied upon perceived results rather than on direct measures for quantifiable dimensions – i.e. profitability and productivity. In future research, financial metrics to provide objective evaluations of a ATMs outsourcing impact on profitability and productivity dimensions should be taken into consideration. Productivity can be measured from the ratios of outputs and inputs. Output is measured through the total revenue, while inputs are measured through the number of employees and the total assets or inventory required to generate the output. Profitability metrics measure the return that banks receive from their investments. This

dimension can be measured by return on assets, return on equity and net profit margin (Jiang and Qureshi, 2006; Smith *et al.*, 1998).

In addition, the respondents in this survey are managers and team leaders who may only evaluate their own branches rather than all the functions of the bank. Thus, it's recommended for future studies that senior managers with an overview of the whole bank be included in the survey for future research. In addition, the results of the study cannot be generalised, as the study was carried out only in a single city. Future studies should therefore cover other branches in the country. Moreover, although this study has looked into relationship between outsourcing and the bank's performance through the perception of managers, it may be appropriate to include other relevant individuals in the process. For instance, employees may evaluate "quality of work life", or customers may evaluate "quality".

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APPENDIX I: LETTER TO RESPONDENT

Dear Respondent,

I am a student at the Kenyatta University, carrying out a survey of the factors that influence the decision to outsource ATM management services at Cooperative Bank of Kenya

Kindly, complete the attached questionnaire giving information that is truthful and accurate as possible. The data obtained herein will be used exclusively for academic purposes only and your responses will be treated strictly confidential. Looking forward to your co-operation.

Thank you in advance.

Yours faithfully,

Researcher

APPENDIX II: QUESTIONNAIRE

This questionnaire is meant to gather information regarding the factors to be considered by Co-operative bank before outsourcing management of ATMs. Kindly respond by ticking in the boxes provided or by writing a brief statement in the spaces provided.

PART A BIOGRAPHIC DATA

1. Please indicate your gender

Gender Male () Female ()

2. Number of service years with the Co-op Bank

i. Less than one year

ii. 1–2 years

iii. 3-5 years

iv. 6-10 years

v. 10+ years

3. For how many years has ATM management been outsourced at your branch?

i 0 years

ii 0–2 years

iii 2-5 years

iv 6-10 years

v 10+ years

PART B: FINANCIAL CONSIDERATIONS IN OUTSOURCING AND THE RELATIONSHIP TO CO-OP BANK'S PERFORMANCE

	Statement <i>Co-op bank has outsourced ATM management services for a number of reasons. Below are statements regarding some financial considerations behind the outsourcing of ATMs. Indicate the extent to which each has made a contribution:</i>	Very High extent	High extent	Moderate extent	Little extent	Not at all
1.	Extent to which ATM management outsourcing has reduced back office processing and maintenance costs					
2.	Extent to which ATM management outsourcing has reduced technology improvements costs					
3.	Extent to which the bank has reduced high fixed costs to variable costs when ATMs are outsourced					
4.	Extent to which costs are spread over a large number of ATMs when ATMs management is outsourced					
5.	Extent to which economies of scale allow third party processors to negotiate attractive pricing through volume discounts that may not be available to the bank					
6.	Extent of increased opportunity cost of capital i.e. free up capital for other important projects					
7.	Extent to which network participation expenses are shared with several other banks outsourcing ATMs to the same provider					

PART C: OPERATIONAL CONSIDERATIONS IN OUTSOURCING AND THE RELATIONSHIP TO CO-OP BANK'S PERFORMACE

	<i>Co-op bank has outsourced ATM management services for a number of reasons. Below are statements regarding some operational considerations behind the outsourcing of ATMs. Indicate the extent to which each has made a contribution:</i>	Very High extent	High extent	Moderate extent	Little extent	Not at all
1.	Extent to which outsourcing increase uptime and reliability of ATMs					
2.	Extent to which outsourcing will allow the bank to leverage new technologies to improve customer service					
3.	Extent to which outsourcing enables adaptation of customized operating platform					
4.	Extent to which outsourcing increases access to greater breadth and depth of ATM management expertise					
5.	Extent to which outsourcing eases data back up and access to better recovery systems.					
6.	Extent to which outsourcing eliminates redundancy of multiple recovery systems					
7.	Extent to which outsourcing has led to the increase in number of new services provided to customers within the bank					

PART D: STRATEGIC CONSIDERATIONS IN OUTSOURCING AND THE RELATIONSHIP TO CO-OP BANK'S PERFORMANCE

	<i>Co-op bank has outsourced ATM management services for a number of reasons. Below are statements regarding some strategic considerations behind the outsourcing of ATMs. Indicate the extent to which each has made a contribution:</i>	Very High extent	High extent	Moderate extent	Little extent	Not at all
1.	Extent to which outsourcing has led to focus on core competencies					
2.	Extent to which outsourcing has led to the increase in levels of utilization of resources increases i.e. in-house staff					
3.	Extent to which outsourcing has led to reduction of customer complaints					
4.	Extent to which outsourcing of ATM management has reduced concerns about quality of service delivery					
5.	Extent to which outsourcing of ATM management has increased competitiveness					
6.	Extent to which outsourcing of ATM management has led to continuous improvement					
7.	Extent to which outsourcing of ATM management reduces operating risks					
8.	Extent to which outsourcing of ATM management improves quality of service					

PART E: RELATIONSHIP BETWEEN OUTSOURCING ATM MANAGEMENT TO CO-OP BANK'S PERFORMANCE

	<i>Co-op bank has outsourced ATM management services for a number of reasons. Below are statements regarding performance of Co-op bank in relation to outsourcing ATM management. Indicate the extent to which each has made a contribution:</i>	Very High extent	High extent	Moderate extent	Little extent	Not at all
1.	Extent to which outsourcing has reduction of costs					
2.	Extent to which outsourcing has increase in revenue					
3.	Extent to which outsourcing has increased productivity levels					
4.	Extent to which outsourcing of ATM management has boosted employee motivation levels					
5.	Extent to which outsourcing of ATM management has ensured repeat customers					
6.	Extent to which outsourcing of ATM management has provided the bank a competitive edge					

THANK YOU FOR YOUR RESPONSE

APPENDIX III: BUDGET

Activity	No. of Units	Unit Cost (Kshs.)	Total (Kshs)
Stationery	-	-	4,200
Typing Cost and Editing	80 pages	30	2400
Photocopying cost	480 pages	3	1,440
Research Assistants' fees	1 person	-	8,000
Consultancy Services	-	-	22,000
Miscellaneous	-	-	6,000
Total Cost			44,040

APPENDIX IV: TIME FRAME

	Feb	Mar	Apr	May
Instrument Design				
Piloting the Instrument				
Revision of Instrument				
Training Research Assistant				
Field Work Activities				
Data Processing				
Report Writing				
Submission of Field Findings report				