INFLUENCE OF COMPETITIVE GENERIC STRATEGIES ON CUSTOMER BASE IN DEPOSIT TAKING MICROFINANCE INSTITUTIONS IN NAIROBI COUNTY

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Abstract

This study was to assess the influence of generic competitive strategies on customer base in deposit taking Microfinance Institutions in Nairobi County. The population of study involved all deposit taking microfinance institutions in Nairobi County according to AMFI report as at 30th August 2013. The target population for this study was top Management and middle level management for all deposit taking MFIs in Nairobi County and the population that had the characteristics to be measured constituted 114 employees of the nine registered deposit taking MFIs in the period as at 20th August 2013 out of which a sample of 92 was selected using stratified random sampling. The study adopted cross-sectional research design and data was collected using questionnaires and analyzed using descriptive and inferential statistics. The study indicated that there existed significant relationship between cost leadership strategy (i.e. $0.002 \leq$ p-value ≤ 0.05) as well as differentiation strategy (i.e. $0.004 \leq$ p-value ≤ 0.05) with customer base at the MFIs on one hand and an insignificant relationship between customer focus strategy (i.e. $0.481 \leq$ p-value ≤ 0.05) and customer base on the other hand. The study recommended that frameworks be established on how to segment the MFIs market, improve the bank's service delivery systems, and identify actionable measures that define marketing, advertisement and communication campaigns as well as improve the quality and accessibility to the bank's products and services.

Key Words

AMFI	Association of Microfinance Institutions
DTM	Deposit Taking Microfinance
KWFT	Kenya Women Finance Trust
MFIs	Micro Finance Institutions
MSEs	Micro and Small Enterprises.
NGOs	Non Government Organizations

1. INTRODUCTION

1.1. Background of the Study

Micro finance refers to the provision of financial services to low-income clients, including consumers and the self-employed. The term also refers to the practice of sustainably delivering those services. Microcredit (or loans to poor microenterprises) should not be confused with microfinance, which addresses a full range of banking needs for poor people. (Ledgerwood, 2000). More broadly, it refers to a movement that envisions "a world in which as many poor and near poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also savings, insurance, and fund transfers." (Robert Richard and Jayadeva, 2004). Those who promote microfinance generally believe that such access will help poor people out of poverty. Microfinance can also be distinguished from charity. It is belter to provide grants to families who are destitute or so poor they are unlikely to be able to generate the cash flow required to repay a loan. This situation can occur, in a war zone or after a natural disaster. Formal credit and savings institutions for the poor have also been around for decades, providing customers who were traditionally neglected by commercial banks a way to obtain financial services through Cooperatives and development of finance institutions. Micro credit and micro finance came into prominence in the 1970s (Robinson, 2001).

Kenyan microfinance marketplace has evolved at a very rapid pace with new entrants, new products and practice, a rise in movement between multiple memberships of financial institutions; and a more demanding and discerning clientele. This has significant implications for the many and various financial service providers operating in this increasingly competitive microfinance market (Dondo, 2001). This increasingly competitive and varied marketplace is beginning to be reflected in a growing number of players. This represents an important change, since until the early 1990s most MFIs did not have to worry about competition. This period of low competition allowed MFIs the freedom to focus single-mindedly on making the breakthroughs in methodology and management necessary for growth and sustainability. However, recent years have seen competition among MFIs growing in leaps and bounds in Kenya. Moreover, donors have questioned the need for continued subsidies, resulting in the recent focus on ‘institutional sustainability’ in the MF sector.

Competitive strategies give any organization a competitive advantage and therefore sell or produce their goods and service in the market than any other business/ company in the market. It is worth noting that in Kenya, there are many MFIs and each one of them has to employ the best competitive strategies to ensure that its position in the market is not taken by the rest. The number of MFIs has considerably increased as the industry has been on the high growth. This has led to saturation in the market and hence increased competition not only in Kenya but in several other countries (Porteous, 2006). It is worth noting that Microfinance Institutions have been used globally to alleviate the lives of the people living in poverty to decent living. This is also associated with successful creation of banking platform through a number of savings, micro insurance, mobile banking, and credit.

1.2 Statement of the Problem

One of the environmental influences to a business is competition and therefore every organization needs a competitive strategy. Increased competition threatens the attractiveness of an industry by reducing the profitability of the players. Firms that do not respond effectively to increased competition are not likely to succeed in business (Porter, 1996). According to a study carried out on competitive strategies, provision of microfinance services that can have a sustainable impact on clients well being and reduced

vulnerability is not an easy endeavor. Microfinance institutions face many risks that adversely affect their long term growth, operational and financial sustainability.
Until the 1990s, most MFIs in Kenya did not have to worry about competition. This period of low competition was essential for the development of microfinance as it allowed them to focus single-mindedly on making the breakthroughs in methodology and management necessary to reach sustainability. These breakthroughs have now brought MFIs to the threshold of competition precipitated by the growth of the industry. MFIs are thus increasingly experiencing competition and it is against this background that this research sought to determine the influence of the competitive strategies that MFIs employ to compete effectively.

1.3 General Objectives

The general objective was on the influence of generic competitive strategies on customer base of MFIs in Kenya.

1.4 Justification of the study

This study will benefit Management of microfinance institutions, the Kenyan government, Development partners, NGO's, Donor communities and other stakeholders as the findings will facilitate crafting of appropriate policies that promotes the growth and stability of the microfinance institutions.

2. LITERATURE REVIEW

2.1 Introduction

This chapter reviews existing literature theories/models advanced by scholars related to the variables, the conceptual framework, empirical studies and critic of the existing literature.

2.2 Generic Competitive Strategies

According to Michael Porter, management must select a competitive strategy that will give it a distinct advantage by capitalizing on the strengths of the organization and the industry it is in. He has argued that a firm's strengths ultimately falls into either cost advantage or differentiation, which applied either broadly or narrowly results in three generic strategies: cost leadership, differentiation, and focus. They are called generic strategies because they are not firm or industry dependent and are applied at the business unit level.

2.2.1 Cost Leadership

Costs are an important determinant of prices charged by firms. It has been argued that companies with lower costs gain competitive advantage by charging lower prices whereas the ability to differentiate allows companies to charge higher prices. Porter (1980) states that characteristics of cost leadership strategy include low level of differentiation, aim for average customer, use of knowledge gained from the past experience and the addition of new products only after the market demands them. Thompson and Strickland (2008) agree with Porter’s view on cost leadership strategies and state that this strategy calls for being the low cost producer in an industry for a given level of quality. Firms acquire cost advantages by improving processes efficiencies, accessing lower cost materials, making optimal outsourcing vertical integration decisions or avoiding some costs altogether. However, the risk of cost leadership is that competitors may leapfrog the technology and production capabilities hence eliminating the competitive advantage acquired from cost reduction. An organization therefore needs to be confident that they can achieve and maintain the number one position before choosing the cost leadership route.

2.2.2. Differentiation Strategy

A differentiation strategy seeks to provide products or services that offer benefits that are different from those of competitors and that are widely valued by buyers.(Johnson, Scholes & Whittington, 2008) The aim of using differentiation strategy is to achieve competitive advantage. A differentiation strategy must be based on two key factors: the strategic customers, the company has to identify their needs and what they will value, and also on the key competitors, to be different, the company has to identify against who it is competing. (Hitt, Ireland, Hoskisson, 2009). The key assumption behind a differentiation strategy is that customers are willing to pay a higher price for a product that is distinct (or at least perceived as such) in some important way. Superior value is created because the product is of higher quality, is technically superior in some way, comes with superior service, or has a special appeal in some perceived way.

Differentiation is often the secret to extending the life cycle of a business and making it more expensive to enter and follow. Firms practicing differentiation seek to design and produce highly distinctive or unique product or service attributes that create high value for their customers. The risks associated with differentiation strategy include imitation by competitors and changing customer tastes and preferences and hence the shelf life of differentiation strategy is getting shorter and shorter.

2.2.3 Customer Focus Strategy

Focus strategy concentrates on serving particular market niche which can be defined geographically by type of customer or by segment of the product line. It is directed towards serving the needs of a limited customer group or a segment hence the company is specialized in some way. The company has enormous opportunity to develop its own niche and compete against low-cost and differentiated enterprises which tend to be larger (Hill and Jones (1999). Firm's can build a focus in one of two ways. They can adopt a cost-based focus in serving a particular niche or segment of the market, or they can adopt a differentiation based focus. Focus strategies are different from low-cost leadership and differentiation strategies in terms of the scope of the target market. Within a particular targeted market or niche, however, a focused firm can pursue many of the target market. Porter stated that the advantages of focus strategy include having power over buyers since the firm may be the only source of supply.

2.3 Empirical Review

McIntosh et al. (2005) examined the effects of competition among MFIs in the Ugandan microfinance market, specifically focusing on its impact on borrower behaviour. He argued that due to increased competition among MFIs in combination with non-existing formal processes of information-sharing between lenders about borrowers' credit history, borrowers would take up more loans from different institutions, leading to a worsening of repayment rates and a reduction of savings.

Lamb and Boyden (1984) carried out a research on challenges influencing application of competitive strategies and identified three competitive challenges that may hinder an organization‘s ability to take advantage of new opportunities. He found that Challenges faced by firms when implementing strategies included lack of financial resources, high cost of borrowing funds, marketing abilities, staff skills, changing customer and external environmental needs, government regulation, and the complexity of coordinating all the firm‘s activities in pursuit of the agreed strategy.

Porter (1998); Ansoff and McDonell (1990) found out that the real challenge in implementing generic strategies was in recognizing all the supportive activities and putting them in place properly. Thompson and Strickland (2002) pointed out that the major fits were between strategy and organizational capabilities; between strategy and reward structures; between strategy and the internal support systems and between strategy and organizational culture. The organization's practices should fit what is required for strategic success in order to ensure that the organization has a unified stand towards the accomplishment of strategy

2.4 Critique of the Existing Literature

Michael Treacy and Fred Wiersema (1993) modified Porter's three strategies to describe three basic "value disciplines" that can create customer value and provide a competitive advantage. They are operational excellence, product leadership, and customer intimacy. Operational excellence means providing customers with reliable products or services at competitive prices and delivered with minimal difficulty or inconvenience. Customer intimacy means segmenting and targeting markets precisely and then tailoring offerings to match exactly the demands of those niches. Product leadership involves producing an ongoing streams of cutting-edge products/services to the customers.

3. RESEARCH DESIGN

The research design for this study was cross-sectional survey as it was based on observations that took place in different MFIs at one time.

3.1 Target Population

The target population for this study was top Management and middle level management for all deposit taking MFIs in Nairobi County. The proportion of the population that had the characteristics to be measured constituted 114 employees.

3.2 Sampling Technique

For this research a total sample size of 92 was adequate. Since 92 was the total sample size required, this was picked as a proportion of 114 using stratified random.

4. PRINCIPAL FINDINGS

4.1 Introduction

The section presents the outcomes of the analysis of the data collected during the study based on the objective, independent and dependent variable, research findings and discussions of the results.

4.2 The response rate

Out of the 92 questionnaires administered, 70 were successfully filled and returned. This represented a 76% response rate. This was considered adequate for analysis.

4.3 Findings

From the findings; cost leadership and differentiation strategy were found to be influencing customer base in deposit taking microfinance institutions while there exists no relationship between focus strategy and customer base in deposit taking MFIs.

4.4 Hypothesis Testing

The study was done under assumption that sampling was undertaken at a significance level of $\alpha = 0.05$. Thus it follows that, at 5% level ($\alpha = 0.05$), the p-values for cost leadership strategy was found to be ($p = 0.002$), differentiation strategy ($p = 0.004$) and customer focus strategy ($p = 0.481$. Two of these variables namely cost leadership strategy and differentiation strategy have critical values and are therefore within the rejection region in a normal distribution curve, while customer focus strategy does not. Consequently, the null hypotheses which state that; H_{01}: Cost leadership strategy has no significant influence on customer base in deposit taking microfinance institutions as well as H_{02}: Differentiation strategy has no significant influence on customer base in deposit microfinance institutions are rejected. However, the null hypothesis which state that: H_{03}: customer focus strategy has no significant influence on customer base in deposit taking microfinance institutions is accepted.

4.5 Summary

From the findings cost leadership strategy and differentiation strategy are significant and good predictors of customer base at deposit taking Microfinance institutions and should be retained in the model, while customer focus strategy is insignificant and a poor predictor of customer base in microfinance institutions.

5. RECOMMENDATIONS

The following are the recommendations from this research study:-

A framework be established on how to segment the bank's market to reduce risk in deciding where, when, how and to whom a product or service should be marketed and increase market efficiency by directing effort specifically toward the designated segment and in a manner consistent with that segment's characteristics.

Establishment of a framework that will help reduce or eliminate waste of time and resources and tackle unnecessary costs, bottlenecks and errors across business processes. This is to be achieved through business process re-engineering with significant improvement in the MFIs service delivery systems.

Implement actionable measures that define accountability for success of marketing, advertising and communication campaigns. This is to be achieved through proper evaluation and measurement of efficacy, performance, cost and impact of integrated marketing activities.

Established a framework that helps in improving quality and access to services in vulnerable customer segments. This is to be achieved through setting service standards, testing for quality of product or service, educating customers and training of employee on customer service and carrying out periodic monitoring of customer satisfaction.

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