THE EFFECT OF STRATEGIC ALLIANCES ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

BY:

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D63/75193/2012

A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF DEGREE OF MASTER OF SCIENCE IN FINANCE, UNIVERSITY OF NAIROBI

OCTOBER 2014
DECLARATION

This project is my original work and has not been presented for and award of degree in any other University.

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This project has been submitted for examination with my approval as University Supervisor:

Signed………………………………….  Date ……………………………………………

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ACKNOWLEDGMENTS

First and foremost, I would wish to thank the almighty God for the free gift of life and for guiding me; giving me strength and the ability to successfully complete this study.

I am deeply indebted to my supervisor Mr. Herick Ondingo from the University of Nairobi whose help, stimulating suggestions helped me during the entire period of this research.

My heartfelt appreciation goes to my dad Mr. William Kilimo, my mum Mrs. Anne Kilimo and my sisters Dama, Chemu and Chep for their relentless support, sacrifices and encouragement during my studies. Their dedication, understanding and vision were surely key to my researching level of my studies.

Finally, I wish to appreciate all my friends who were always there for me.

To all of you, I say God bless you.
DEDICATION

This project is dedicated to my dad Mr. William Kilimo, my mum Mrs. Anne Kilimo, my sisters Damaris Kilimo, Faith Kilimo, Ruth Chepkoech, my gorgeous nephew Gavin Mnang'at and finally my brother in law Poriot Daimoi for their encouragement and support during the time of my studies.
ABSTRACT

The advent of globalization coupled with a competitive business environment has seen many organizations opt for different strategies for survival. Today, the strategy of allying with other organizations has become increasingly prevalent with many organizations opting for strategic alliances in order to strengthen their market positions and improve on their financial performance. In Kenya, where the banking industry is cut throat competition, financial institutions have had to adopt a myriad of strategies in order to gain competitive advantage and stay afloat in the market. Of concern to the study, was how the proportion of funds set aside for strategic alliances, financial leverage and size of commercial banks influenced their financial performance which was measured by the rate of return on assets. The study was a descriptive design, targeting 43 commercial banks. Document analysis was used to collect data from bank statement of financial performance and statements of comprehensive income during the period 2009-2013 while General Economic Data was collected from the site of the Central Bank of Kenya. Data was analyzed using Statistical Packages for Social Sciences (SPSS) version 17. Regression and correlation analysis were used to determine the nature and the strength of the relationship between the independent and dependent variables. The findings of this study reveal that all the commercial banks in Kenya were involved in at least one form of strategic alliances. On average, the banks were in at least three strategic alliances. Correlation analysis carried out between the study variables yielded a value of R is 0.747 an indication that a strong relationship existed between the variables. There was a strong positive relationship between performance of commercial banks, proportion of funds set aside for strategic alliances and bank size. A strong negative correlation exists between financial performance and financial leverage. The study also found out that there exist a positive correlation between bank size and the proportions of funds set aside for strategic alliances. Therefore, in order for commercial banks to enhance their financial performance, there is need to increase their engagement into strategic alliances. Although not conclusive, the results of this study lay foundation for potential future research and useful recommendations for the policy direction. Some of the limitations encountered have also been highlighted.
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<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>CBK</td>
<td>Central Bank of Kenya</td>
</tr>
<tr>
<td>DPS</td>
<td>Dividend per Share</td>
</tr>
<tr>
<td>EBIT</td>
<td>Earnings before interest and taxes</td>
</tr>
<tr>
<td>GEPS</td>
<td>Growth Earning per Share</td>
</tr>
<tr>
<td>IJV</td>
<td>International Joint Ventures</td>
</tr>
<tr>
<td>JV</td>
<td>Joint Venture</td>
</tr>
<tr>
<td>KPMG</td>
<td>Klynveld Peat Marwick Goerdeler</td>
</tr>
<tr>
<td>MTO</td>
<td>Mobile Transfer Operators</td>
</tr>
<tr>
<td>P/E</td>
<td>Price/Earning</td>
</tr>
<tr>
<td>ROA</td>
<td>Return on Assets</td>
</tr>
<tr>
<td>ROCE</td>
<td>Return on Capital Employed</td>
</tr>
<tr>
<td>ROI</td>
<td>Return on Investment</td>
</tr>
<tr>
<td>ROS</td>
<td>Return on Sales</td>
</tr>
<tr>
<td>SPSS</td>
<td>Statistical Package for Social Science</td>
</tr>
<tr>
<td>USA</td>
<td>United States of America</td>
</tr>
<tr>
<td>WOS</td>
<td>Wholly Owned Subsidiaries</td>
</tr>
</tbody>
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CHAPTER ONE
INTRODUCTION

1.1 Background of the Study

In recent years considerable attention has been devoted to the formation of strategic alliances. Strategic alliances have been seen as an important part of sustainable development plan for corporate. Nevertheless, many of studies estimate that most of strategic alliances end being dissolved. For example, The Economist (1999) reveals that two-thirds of all inter-organizational strategic alliances formed between 1992–1995 were dissolved.

This high failure rate of alliances has placed major emphasis on developing robust alliance formation guidelines and processes, as well as attempting to identify what types of firms form effective alliances and the underlying rationale (Cravens, Cravens and 2000). The Business Week (1999) reports that a major reason for the high failure rate of alliances is that only 31% of organizations develop and implement formal performance measures, and only one in five executives considers the measures implemented as being reliable indicators of the success of an alliance (Business Week, 1999). According to Cravens et al (2000), lack of reliable performance indicators is probably associated with the lack of general consensus regarding the requirements for a successful alliance, and major disagreement on appropriate measures to assess performance.

Recently, the most emerging practices amongst financial institutions has been that of forming strategic alliances with organizations such as brokerage firms, investment banks and mobile providers. Berger, Demsetz, and Strahan (1999), Boot, Milbourn, and Thakor, (1999) indicate that financial services firms will continue to strategically position
themselves in order to gain competitive advantage in the ever evolving competitive marketplace.

In Kenya, the banking sector is a cut-throat business arena, with over 44 players among them are multinationals all scrambling for a slice of the market share. Although the industry has been experiencing rapid growth in terms of profits, deposits and revenues in the past decade, stiff competition has been the norm for the industry. This has necessitated all the players to device new approaches in order to create and maintain a competitive advantage Equity Bank’s (The Market, 2011).

1.1.1 Strategic Alliances

The importance of strategic alliances in today’s business environment has been a common point of discussion in the world of academia. At the same time, strategic alliances are becoming more and more prominent in the global economy. Strategic alliances are fast becoming a trend in the corporate business. In fact, the biggest change in corporate culture and the conduction of business is the rapidly growing number of corporate deals based not on ownership, but on partnerships (Drucker, 1996). Indeed, searches on the internet for strategic alliances produces numerous press releases of companies forming alliances and also produce several addresses for strategic alliances consulting companies. According to Booz and Hamilton (1997), the number of strategic alliances had double in a decade and was expected to increase tremendously. Farris (1999) reveals that in 1998 alone more than 20,000 corporate alliances had been formed globally.
According to Mockler (1998), strategic alliances are “agreements that are important to the partners, created to achieve common interests”. Amita, Pearce, Richard and Robinson (2011) define a strategic alliance as an agreement between two or more companies in which they both contribute capabilities, resources or expertise to a joint undertaking, usually with an identity of its own, with each firm giving up overall control in return for the potential to participate in and benefit from the joint venture relationship. According to Wheelan and Hungar (2000), a strategic alliance is an agreement between companies to establish cooperative partnerships that go beyond normal company-to-company relations, but fall short of becoming a real merger. Gamble, Strickland and Thompson (2007) on the other hand define a strategic alliance as a formal agreement between two or more separate companies in which there is strategically relevant collaboration of some sort, joint contribution of resources, shared risk, shared control and mutual dependence.

Alliances include a wide variety of goals which companies are completely or partially precluded from achieving when confronting competition on their own. Strategic alliances range from simple, informal “handshake” agreements occurring over lunch to formal agreements complete with contracts that enable companies to exchange equities (Elmuti and Kathawala, 2001). Different sets of reasons can be found as to why a firm should seek strategic alliances in order to compete in today’s open and aggressive markets. Gamble et al (2007) stipulates that globalization and technical advances in the world are major causes for companies advocate for strategic alliances so as to become global market leaders. Firms use the alliances as an entry strategy to new markets by partnering with existing companies in that market arena.
According to Amita et al (2011) strategic alliances enable companies to extend their strengths to competitive arenas that they would otherwise be hesitant to enter alone. These companies benefit from one another in areas such as marketing, distribution, production, research and development, and outsourcing. When companies form alliances, they are able to accomplish bigger projects quickly and profitably. According to Barney (2002), strategic alliances may take three forms - joint venture, equity alliances and non-equity alliances. Scholars such as Knoke (2001) also include: hierarchical relations, cooperatives, Research and Development consortia, strategic cooperative agreements, cartels, franchising, licensing, subcontractor networks, industry standards groups, action sets and market relations as other forms of strategic alliances.

1.1.2 Financial Performance

Olubukunola (2011) defines financial performance as the measure of how well a firm can use assets from its primary mode of business and generate revenues. The term is also used as a general measure of a firm's overall financial health over a given period of time. According to Srinivas (2013), financial performance refers to the act of performing financial activity. In other words, the degree to which financial objectives are being or have been accomplished. It is the process of measuring the results of a firm’s policies and operations in monetary terms. It is used to measure firm's overall financial health over a given period of time and can also be used to compare similar firms across the same industry or to compare industries or sectors in aggregation.

A company’s financial statements provide various financial information that investors and creditors use to evaluate a company’s financial performance. This usually entails the growth and profitability of a company (Hill, Murphy and Trailer, 1996). Collins and
Jarvis (2006) posit that the most useful sources of the financial performance of a firm are the periodic management account such as the balance sheet and income statement, cash flow information and bank statements. They estimate that these of information are used by over 80% of companies to determine their business performance.

The core of business enterprises is to make profit in the short-term while in the long run is to increase the owner’s wealth. Financial measures being quantitative, objective, scientific and intuitive are mostly proffered in measuring the financial performance of organisations. Traditionally, financial performance measures are split into those measuring; profitability, liquidity/working capital, gearing and investors ratios (Kaplan, 2012).

Profitability measures include: return on capital employed (ROCE), which is a key measure of profitability showing the net profit generated from every shilling of assets employed. The ROCE can be understood further by calculating the net profit margin and the asset turnover; asset turnover (this is the turnover divided by the capital employed) which shows the turnover that is generated from each shilling of assets employed, Ready Ratios (Audit IT, 2013)

Some of financial measures for management performance and stockholders wealth evaluation are: operating income, earnings before interest and taxes (EBIT), net asset value, return on equity (ROE), return on investment (ROI), return on sales (ROS), growth earning per share (GEPS), price/earning (P/E), and dividend per share (DPS) (Rahnemae, 2006). In banks, there are many different of measuring the financial performance and this includes return on assets (ROA), return on equity (ROE) and net interest margin
(NIM) (Karina, 2012) It is still important to note that no one measure of financial performance should be taken on its own rather a thorough assessment of a company’s performance should take into account many different measures.

Return on Equity is what shareholders look in return for their investment. A business that has a high return on equity is more likely to be one that is capable of generating cash internally. Thus, the higher the ROE the better the company is in terms of profit generation. Its further explained by Khrawish (2011) that ROE is the ratio of Net Income after taxes divided by Total Equity Capital.

Return on Equity = Net Income / Equity Capital

Return on Asset is another ratio that indicates the profitability of a bank. It measures the ability of the bank’s management to generate income by utilizing company assets at their disposal in other words, it shows how efficiently the resources of the company are used to generate income. It’s the ratio of income to its total assets (Khrawish, 2011)

ROA = Net Income /Total Assets

1.1.3 Effect of Strategic Alliances on Financial Performance of Firms

In a study carried out by KMPG (2009) on Joint ventures, the study revealed that strategic alliances were on the rise. Companies forming joint ventures had specific reasons for opting for the ventures. The main reasons for the formation of strategic alliances were so as to enable the companies gain access to greater markets, reduce on costs, reduce risk as joint ventures can share or spread risk between partners better than alternative forms of corporate strategies hence improving on their profitability (KPMG, 2009). In highly uncertain foreign markets in particular, international Joint ventures
(IJVs) tend to outperform wholly owned subsidiaries (WOSs) because of the benefits a local partner provides (Brouthers, 2002). Unlike non-equity alliances, the capital invested in a JV signals partner commitment, thereby enhancing the probability of success. This commitment enhances cooperation among the parent firms, which is especially important when they are competitors, as is sometimes the case (Beamish and Lupton, 2009).

Craig (2005) on the other hand reveals that despite strategic alliances offering the promise of economic and other benefits, they often entail significant costs in their implementation. Due to their shared decision making nature, strategic alliances tend to be fragile relationships with a high failure rate; above 305 according to Beamish and Makino (1998), Park and Ungson (1997) among others. Lane and Beamish (1990) found out that breakdown of communications generally had significant consequences on strategic alliances which sometimes led to the eventual dismemberment of the venture.

1.1.4 Commercial Banks in Kenya

The banking sector plays a very crucial role in the economy by facilitating the flow of money from depositors to borrowers. Thus banks receive money from customers and lend it out to customers in form of loans. The role of banks in an economy is paramount because they execute monetary policy and provide means for facilitating payment for goods and services in the domestic and international trade (GOK, 2007)

The Companies Act, the Central Bank of Kenya (CBK) Act and the Banking Act are the main regulators and governors of banking Industry in Kenya. These Acts are used together with the prudential guidelines which Central bank of Kenya issues from time to time. In 1995 the exchange controls were lifted after the liberalization of the banking in
Kenya. Central Bank of Kenya is tasked with formulating and implementation of monetary and fiscal policies and it the lender of last resort in Kenya and is the banker to all other banks. The CBK ensures the proper functioning of the Kenyan financial system, the liquidity in the county and the solvency of the Kenya shilling. To address issues that affect the Banking industry in Kenya, banks have come together and formed a forum under the Kenya Bankers Association.

The financial industry in Kenya, especially the banking sector plays a crucial in the growth of Kenya’s economy. The industry has been one of the fastest growing not only in the East African region but in Africa. Between 2002 and 2012 the total assets in the industry grew from Ksh.456.7 billion to Ksh.2.35 trillion, total deposits grew from Ksh 360.6 billion to Ksh 1.76 trillion and net advances increased from Ksh 222.8 billion to Ksh 1.27 trillion. Within the same time the number of bank accounts increased from 1.9 million accounts to 17.6 million with deposit insurance having evolved and covers fully over 94% of the total deposit accounts (CBK, 2013)

According to Lovstal (2011), the major driving force for strategic alliances is to enable firms gain a competitive advantage, thereby increasing profitability. As firms combine resources, this often leads to the attainment of synergy where the new arrangement may lead the firms to perform a service more efficiently, produce a product at a less cost or utilize a facility or funds more effectively. This ultimately results in greater profits for the firms involved than they would have achieved as separate business entities. Financing is also a common goal of strategic alliances: financial is what brings in banks into alliances with non-financial institutions such as mobile service providers or technology providers at large. Smaller firms in particular tend to benefit from the usually better financial
positions of larger firms. In addition, strategic alliances offer a better chance of obtaining credit or raising more equity as creditors and investors’ confidence in the new firm is often greater. As a joint entity, they provide better guarantee for creditors fund as their assets base is widened (Lovstal, 2011). Strategic alliances also provide firms with an efficient means for acquiring and exchanging complementary knowledge (Hennart, 1988).

Due to changes in the operating environment, several licensed institutions, mainly commercial banks, have had to join their operations in mutually agreed terms where these institution do business jointly (Brito, Pereira, and Ribeiro, 2008). Some of the reasons put forward for these alliances has been to meet the increasing market demand and competition, diversify to international markets, employ the emerging new and expensive modern technologies, or to meet the new threshold capital required by the regulators such as in the banking sector (Kithinji and Waweru, 2007).

1.2 Research Problem

According to Kimberley, Ike and Roy (2003), whereas there exist an extensive body of literature that examines mergers, acquisition, and consolidation activity in commercial banks and other financial services firms, little attention has been paid to examine the practice of strategic alliances within commercial banks. Kumar (2005), in study titled, ‘The value from acquiring and divesting a joint venture: A real options approach’, examines the value created from acquiring and divesting in a joint venture. Even though Kumar (2005) gives benefits of Joint ventures, the study examines value in light of the reason behind terminations of JV and the characteristics of the target market, failing to look at the financial performance of the terminating firms during the period of the joint
ventures. Nevertheless, the author recommends that it may be useful to conduct a study of the value associated with strategic alliances.

Several authors have identified potential problems and challenges that might lead to failure in strategic alliances. Bamford, Ernst and Fubini (2004) have highlighted various reasons for failure including: wrong strategies, mistrust, incompatible partners, inequitable or unrealistic deals, weak management, inadequate launch planning and execution among others. Harrigan (1985) points out that many strategic alliances failures can be attributed to compatibility problems between the firms. These might include partners of unequal size, collaboration experience, or managerial style. Other incompatibilities include staffing errors and the lack of participatory management. Spranger (1991) argues that most strategic alliances are doomed to failure from their inception due to insufficient planning, inadequate capitalization, lack of leadership, lack of commitment and cultural and ideological differences.

Many studies have been done in the area of strategic alliances and the results found from the studies have been inconsistent. Musyoki (2003) studied the creation and implementation of strategic alliances among non-governmental organizations with a case of Gedo health consortium. Wachira (2003) carried out a survey on strategic alliances in pharmaceutical drug development, a case study of three strategic alliances at Eli Lilly and company. Koigi (2002) carried out a survey on the implementation of strategic alliance experience of Kenya Post Office Savings Bank (KPOSB) and Citibank. Kamanu (2005) emphasized that strategic alliances among development of NGOs in Kenya are a crucial component in the success of any organisation for profit or non-profit in the world today.
Kavale (2007) did a study on strategic alliances in a mobile money transfer as relates to the banking industry.

This study while based on a similar conceptual argument as noted in the above local studies is differentiated in the sense that it looked at strategic alliances in the banking industry in Kenya. It was based on the drivers of the alliances similar to the study conducted by Mutinda (2008). The study explored the factors which have driven banks to strategic alliances and the challenges they are experiencing. This study intends to address the following Research Question: What is the effect of strategic alliance on the financial performance of commercial banks in Kenya?

1.3 Research Objective

To determine the effect of strategic alliance on the financial performance of commercial banks in Kenya.

1.4 Value of the Study

In Kenya, the field of strategic alliances is one that has not been extensively researched. This study will be important as it will contribute greatly to the limited number of studies on the subject. The findings of the study will act as a guide to policy makers in analyzing the effect of strategic alliances on the financial performance of banks and in analyzing ways in which banks can make best use of strategic alliances in order to improve their financial performance. The result of this study will also provide other financial institutions with information on the importance of joint ventures which they can use to enhance their performance. Considering that there is minimal work on joint ventures in
commercial banks, will contribute to the general body of knowledge and form a basis for further research to academicians.

The scrutiny of the overall performance of the banking sector is important to depositors, owners, potential investors and the policy makers as banks are the effective executors of the monetary policy of the government. Ownership structure as an internal mechanism of corporate governance is an area of study that has elicited different views on the same operational variables affecting performance. This study therefore is an important empirical reference for the finance literature in the area of Joint Venture.

The study is also important in giving insight on strategic alliances of the Commercial Banks in Kenya and will help those set policies that would ensure that there ownership structures create value for their institutions. It also shows the different owners the importance of their monitoring capability on the financial performance of the Commercial Banks they own.
CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews the literature on strategic alliance giving its definition and several cases of strategic alliance with commercial banks, the reason for the alliances and the challenges encountered. The literature is provided in line with the research objectives. The theoretical underpinnings of the study and the conceptual framework will also be highlighted in this chapter.

2.2 Theoretical Review

Various metaphors have been used to describe the phenomenon of strategic alliances. According to Baran, Pan and Kaynak (1996) the arguments in favour of corporate alliances fall into various schools of thought. Three schools of will be utilized in this study: the Knowledge Based Theory, the Resource Dependence Theory and the Transaction Cost Theory. These schools of thought contribute to our understanding of strategic alliances from different perspectives and are the theoretical underpinnings for this study.

2.2.1 Knowledge Based Theory

As indicated by Steensma and Lyles (2000), knowledge-based perspective is particularly applicable to the study of strategic alliances. Efforts to build the knowledge-based theory of the firm also draw on the evolutionary theory of economic change proposed by Nelson and Winter (1982). According to this theory, a firm is a social entity, which evolves by adapting the body of knowledge shared by its members, and it is the firm’s productive knowledge that defines its competitive advantage.
Critics of knowledge based theory mainly focus on whether it is sufficient to explain a firm’s behavior. It is not possible to tell why firm exist in the absence of ‘opportunism’ or ‘moral hazard’ (which is the basic premise of the contractual approach) (Foss, 1996, 1996). Moreover, it can neither explain firm’s boundary nor identity because what happen between firms is similar to what happen within firms (Eisenhardt and Santos, 2002).

In this study, the proliferation of strategic alliances will be viewed as one driven by the knowledge based theory. Since strategic alliances occur when two or more partners pull resources together to establish an alliance, then the firms have a knowledge base that is not diffused across their boundaries. This becomes the driving force of strategic alliances, more so as a means of transferring tacit knowledge. For organizational embedded knowledge, such as organizational routines, the transfer is difficult unless the organization itself is replicated. Thus, the main reasons to strategic alliances is because one or both the firms desire to acquire the other’s organizational know-how; or one firm wants to retain its organizational capability while benefiting from the other firm’s knowledge. This benefit to a firm can only then be realized in improved performance of the firms leading to profitability; which to any organization is financial.

2.2.2 The Resource Dependence Theory

This theory was developed by Emerson (1963) and further progressed by Pfeffer and Salancik (1978), who proposed that control over critical resources by one organization can make other firm dependence on it. Resource Dependence Theory assumes that even operating in the same industry, firms are heterogeneous in terms of their resources and capabilities. In essence, the theory argues that organizations are often not self sufficient
for all the needed resources that can enable them remain competitive. Therefore they need to engage in exchanges with other organizations in one way or the other so as to gain necessary resources for survival. This usually makes a strategic alliances a viable form of inter-organizational structure that can minimize uncertainties thus enhancing access to much needed resources (Gray and Yan, 1992).

Resource dependence theory has emerged as an important explanation for the persistent firm level performance by emphasizing firm’s ability to create and sustain competitive advantage by acquiring defending advantageous resources positions (Leiblein, 2003). The competitive advantage of a firm is the result of a strategy that utilizes its unique resources and skills. The application of resource dependence theory will deepen our understanding of what resources parent firms prefer to control and how they control them.

2.2.3 The Transaction Cost Theory

The basic tenet of the Transaction Cost Theory is based on the assumption that markets at times fail to allocate factors services and goods efficiently due to among others, natural and government-induced externalities (Kogut 1988). This in turn results in higher costs of organizing exchange through market than organizing exchange internally. These costs are usually referred to as natural externalities, ownership externalities, and technical externalities and so on. Strategic alliances come in to bring the transactions of these cost under a common cooperative structure thereby enabling the partners to reduce the cost involved hence avoiding opportunism among exchange partners (Beamish and Bank, 1987). According to Hennart (1988), the equity link between strategic partners and their ventures is preferable to coordination through spot markets or contracts. This theory has
been applied in explaining the choice of strategic alliances as a business option for commercial banks.

2.3 Determinants of Financial Performance in Banks

Banks performance reflects an organization’s understanding and knowledge regarding customer’s needs and expectations. Adeoye and Olukemi (2012) in their study on Islamic banking practices found that there’s a positive correlation between financial performance of commercial banks and customer satisfaction. Financial performance is a measure of a bank’s policies and operations in monetary terms. It is a general measure of a firm’s overall financial health over a given period of time and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation. Most studies conducted in relation to bank performance focus on sector-specific factors that affect the overall banking sector performances (Chantapong, 2005; Olweny and Shipho, 2011; Heng et al, 2011). Nevertheless there is a need to include the macroeconomic variables.

Profit is the ultimate goal of commercial banks. All the strategies designed and activities performed thereof are meant to realize this grand objective. However, this does not mean that commercial banks have no other goals. Commercial banks could also have additional social and economic goals. However, the intention of this study is related to the first objective, profitability. The profitability analysis is achieved on a set of indicators to measure the banking financial performance. The indicators result from accounting dates which illustrate the reference periods in the most synthetic expression of balance sheet and the profit & loss account (Pagano, 2001).
The determinants of bank performance can be classified into bank specific (Internal) and macroeconomic (External) factors (Al-Tamimi, 2010; Aburime, 2005). These are stochastic variables that determine the output. Internal factors are individual bank characteristics which affect the bank’s performance. These factors are basically influenced by internal decisions of management and the board. The external factors are sector-wide/country-wide factors which are beyond the control of the company and affect the profitability of banks.

Financial performance can be evaluated using many financial indicators such as liquidity ratios, management performance, and leverage among others. There are many different ways to measure a bank’s financial performance and this includes return on assets (ROA), return on equity (ROE) and net interest margin (NIM). Return on equity (ROE) refers to how much profit a company earned compared to the total amount of shareholder equity invested or found on balance sheet.

2.3.1 Strategic Alliances

Elmuti and Kathawala (2001) posit that Strategic alliances can be effective ways of diffusing new technologies rapidly, entering new markets, bypassing government restrictions expeditiously, and learning quickly from the leading firms in a given field. Nevertheless, they are not easy to create, develop and support. Strategic alliances usually fail because of tactical errors made by the management. By using a well-managed strategic alliances agreement, organizations can gain significantly in markets that would otherwise have been uneconomical. Therefore, considerable amount of time and energy must be put in order to create a successful alliance. It is essential for corporations to enter in strategic arrangements with a comprehensive plan that outlines the expectations,
requirements and expected benefit of the alliance (Elmuti and Kathawala, 2001). Harrigan (1985) observed that strategic alliances are not only used by firms to exploit peripheral markets or technologies, but are being perceived increasingly as critical elements of an organization’s business units network as strategic weapons for competing within a firm’s core markets and technologies.

According to Buckley and Casson (1988), strategic alliances facilitate inter-firm learning with successful ones creating synergy and enhancing economic rents to their partners as the result of risk reduction, economies of scale and scope, production and rationalization, convergence of technologies and better local acceptance. However, despite their increasing importance, strategic alliances have often encountered problems of unsatisfactory performance (Geringer, 1986). The primary problem in managing strategic alliances stems from the presence of two or more parents. The conflict between the partners due to incompatible management styles and approaches, differences in organizational culture of the partners and differences in national culture between the home and host country can hamper the performance of strategic alliances.

2.3.2 Cultural Differences

Entering a foreign country through an international strategic alliance has several advantages compared to entering through a wholly owned subsidiary. The international strategic alliance allows the firm to share the cost and the risk of foreign entry and to use the local partner knowledge about the local institutions framework, local consumer tastes and business practices, Agarwal and Ramaswami (1992). However, international strategic alliances also entail unique risks owing to the potential problems of cooperating with a partner from a different national culture. According to Brown, Rugman and Verbeke
(1989) the cultural difference may create ambiguities in the relationship which may lead to conflict and even dissolution of the venture. However, some differences in cultural backgrounds may be more difficult to combine than others.

2.4 Review of Empirical Studies

According to Robert (1998), the proliferation of joint ventures is being driven by a multiplicity of forces, often with powerful and surprising results: Global economic and competitive forces have transformed the nature of some industries. Converging technologies and markets have been another primary factor in the formation of JV. Systems Integration has spurred the creation of numerous joint ventures as increasingly sophisticated technologies have required closer coordination of their research, development, and customer application. For example, in the financial services industry, joint ventures are proliferating to better link the customer electronically with investment services, benefits processing, bundled services, and cash access. Value migration coupled with globalization has also played a role in compelling companies to engage in joint ventures so as to enable them gain a position in emerging markets. Globally, 40% of all breakthrough technology development occurs through collaborative technologies. Hence, the need for innovative Technologies has spawned numerous strategic alliances (Robert, 1998).

2.4.1 International Evidence

Because the subject of how a foreign firm enters a country has been central in the literature on the international activities of the multinational enterprise, there is a longer history of studies on strategic alliances in the field of international business. These studies are especially important because, unlike the domestic studies, a few have
investigated the choice of joint ventures among other alternatives for entry. Many of these studies have examined the use of strategic alliances as a response to governmental regulations, especially in developing countries, through an analysis of a few cases (Tomlinson, 1970; Friedman and Kalmanoff, 1961). Though the case studies are of unquestionable interest, we focus primarily upon studies statistically analysing entry decisions.

Vennet (1996), using a sample of 422 domestic and 70 cross border acquisitions of European Community (EC) credit institutions that occurred over the period 1988-1993 to examine the performance effects of mergers and acquisitions noted that where domestic mergers occurred among equal-sized partners, the merger significantly increased the performance of the merged banks. He also found improvement of cost efficiency in cross-border acquisitions whereas domestic takeovers were found to be influenced predominantly by defensive and managerial motives such as size maximisation.

In a study on determinants of joint venture performance in a developing country, Sim and Yunus (1998) found out that parents’ companies past strategic alliance experiences, complementary resources, and cooperation between the parent companies were important determinants of success of a strategic alliance. At the same time, parent firm-related, industry related, managerial and parent country related factors all have impact on strategic alliances performance. The strategic alliance experience, extent of linkages and relatedness and resource complementarily. Managerial factors and firm-related factors that were found to have an impact on the performance of strategic alliances were relative firm size, extent of multinationality, such as control, operational autonomy and cooperation were key variables in financial performance with Key industry-related
factors relevant to a developing country being the technology level and market (export) orientation (Sim and Yunus, 1998).

Thair, Ahoud and Razan (2011), researched on the effect of the banks characteristic, competitive environment, economic conditions, regulation, legal environment and other factors such as religion on the banks performance. The banks characteristics included banksize (measured by total assets), size and duration of loans, concentration in lending activity, bank capital and its capital structure and the banks operating cost. They considered this the most important variable in the study which had the highest influence on performance as it affected its ability to attract and retain customers who were the main revenue drivers. Their results suggested that commercial banks in the Middle East region should concentrate on the six factors, in order to improve their performance and compete efficiently with global commercial banks.

2.4.2 Local Evidence

Chesang (2002), while studying on merger restructuring and financial performance of commercial banks in Kenya, concluded that though some banks showed a decline in performance in the alliance period, merger restructuring could still be considered as a recommended option to improve the overall financial performance of weak and ailing small and medium sized banks with a narrow business. She noted that merger restructuring is likely to positively affect financial performance due to renewed attention to new business growth strategies, improved management, accounting and reporting systems, legal regulatory systems, better credit assessments and reduced staffing levels. These operational efficiencies are likely to achieve higher rates of return for the merged firm.
Rotich (2005), in his study concluded that the profitability of commercial banks depends heavily on the net of income generating activities and the related activities expense. Due to the problem of profitability and stiff competition in the industry, commercial banks have changed their behavior of income sources, by increasingly diversifying into non intermediation income generating activities as opposed to the traditional inter-mediation income generating activities. The objective of this paper was to establish the impact of income source diversification on financial performance of commercial banks in Kenya. The researcher found out that banks performance heavily improved when it enhanced its ability to generate income from non-interest income components. Further the analysis revealed that non-interest income components fees and commission on loans and advances are highly correlated with interest income. The two revenue streams (interest and non-interest income) are highly and positively related implying that they move in same direction and can be affected by same shock. This is not surprising as non-intermediation activities begs a lot on intermediation or banks traditional activities and thus the two streams cannot be substituted for each other.

Gichuhi (2011) conducted a study on Joint Venture for Construction of Houses in Kenya. From his findings, the concept of Joint Venture for construction of houses is relatively new in Kenya. This method works well for properties designed for sale. Francis explains that in this Joint Venture, the Land owner contributes the land as part of his/her contribution, then the commercial banks contributes finances for construction. The profits are then split on a pre-agreed ratio with the land owner usually getting over 50% of the net profits. In Kenya, Shelter Afrique bank finances strategic alliance projects. For the
projects to be eligible for the financing, a Feasibility study carried out by a registered architect, quantity surveyor or valuer must be present. This feasibility study should show critical minimums such as Return on Investment, target market and land value ratio to the total project cost. These critical features will be used to check if the project is viable as strategic alliance.

2.5 Summary of Literature Review

Despite the popularity of strategic alliances in international business, a considerable proportion of joint ventures are unstable or performed unsatisfactorily. Further, the rates of instability and unsatisfactory performance are relatively higher in developing countries than in developed countries (Sim and Yunus, 1998). Nevertheless, many of the studies undertaken on strategic alliances in both the developed and developing countries only take into account a small number of factors that may positively influence strategic alliances outcomes with the effect of strategic alliances on the financial performance of financial institutions far from clear. Some of the studies even reported contradictory impacts. The effect of strategic alliances on financial performance of commercial banks has not been deeply investigated with some authors such as Gleason et al. (2006) comparing the result of deals joining banking or non-banking partners, while others such as Marciukaityte et al. (2009) contrast the case of financial and non-financial partners. This paper could be among the first in the country to seek to address the effects of strategic alliances on the financial performance of commercial banks.
3.1 Introduction

This chapter forms the research methodology and discusses the methodological and research approaches that were used in the study. In particular, the chapter looks at the research design, the sample and sampling procedures, data collection instruments, data collection methods and the data collection techniques that were used to meet the research objectives.

3.2 Research Design

According to Gerhard (2004), a research design is way a study is designed or the method used to carry out the research. Design involves planning, organizing, collection and analysis of data to provide information and also solutions to the existing problem of the study.

A descriptive research design was used. It helps in providing answers to the questions of who, what, when, where, and how associated with a particular research problem; a descriptive study cannot conclusively ascertain answers to why. Descriptive research is used to obtain information concerning the current status of the phenomena and to describe "what exists" with respect to variables or conditions in a situation. The goal of the descriptive study is to offer the researcher a profile or to describe aspects of phenomenon of interest from an individual/organizational industry oriented and other perception. To achieve the proposed research objective of investigating the effects of strategic alliances on the financial performance of Commercial Banks in Kenya, a
descriptive study was adopted. Gerhardt (2004) considers this method as being the most efficient and most cost-effective research method.

3.3 Target Population
The target population for this research was all the commercial banks operating in Kenya which consists of 43 banks as indicated in the Appendix 1. The study thus adopted a census approach.

3.4 Data Collection
Collis and Hussey (2003) posit that any data needed for a study can only be collected either as secondary data or as primary data. Primary data is that which is collected at source while secondary data is that which is already in existence. For purposes of meeting the research objectives, both primary and secondary data were used. The study adopted the use of a questionnaire and a document analysis as the main research instrument. Document analysis was carried out through desk research and involved a review of literature such as reports, financial statements, books and journals.

The population of this study was all 43 commercial banks in Kenya that have had complete set of data for the periods 2009-2013. Bank level data was collected from bank statement of financial performance and statements of comprehensive income during the period 2009-2013. General economic data was collected from the site of the Central Bank of Kenya.

3.5 Data Analysis
The research adopted both quantitative and qualitative approaches, implying that both descriptive statistics and inferential statistics were employed. Quantitative data collected
from the document analysis was analyzed statistically using the Statistical Package for Social Scientist (SPSS) version 17.0. All qualitative gathered during the study was analyzed through content analysis and was presented descriptively. Microsoft Excel 2007 was used to generate charts from the data analyzed by SPSS. The results of the study are presented in tables.

3.5.1 Analytical Model

The model of our study is presented as follows:

\[ Y = \beta_0 + \beta_1 PSA + \beta_2 SZ + \beta_3 LEV + \varepsilon \]

- \( Y \) - Financial Performance of banks measured by ROA (net income/total assets)
- \( PSA \) - Proportion of funds that the bank has put in the Strategic Alliance
- \( LEV \) - Leverage measured by debt/equity
- \( SZ \) - Size of the bank as measured by the natural log of the book values of the assets
- \( \beta_0 \) - Constant
- \( \beta_1, \beta_2, \ldots, \beta_N \) - Coefficients of Variations

Regression Analysis was used to determine the value the financial performance for the banks prior and after the joint ventures. Correlation analysis based on the y-value was utilized in determining the relationship between the two values.

3.5.2 Test of Significance

The study will test the level of statistical significance of the findings of at 5% using the Analysis of variance technique (ANOVA). A 5% level of significance is another way of saying that 95% of the time that a sample is taken from the population, the study will be likely to generate the same results. The ANOVA solves the difficulty that arises with
either z-test or t-test when examining the significance of the difference amongst more than two samples at the same time. Where results of the test fall within the 5% level of significance, it means that the sample selected is a true representation of the population.
CHAPTER FOUR
DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter presents the research findings and interpretation of study data. The research study was descriptive in nature and aimed at establishing the effect of strategic alliances on the financial performance of commercial banks in Kenya. The study targeted all the commercial banks in Kenya. Data was collected through both primary and secondary data. While questionnaires helped gather primary data, document analysis acted as the source of secondary data for the study. The data analysis for this study was carried out through descriptive and content analysis. Pearson correlation and regression analysis were adopted to evaluate the degree of association between variables and in estimating their existing relationships. Analysis of variance (ANOVA) was used to measure the differences and similarities between the sample banks according to their different characteristics. The results of the study are presented in tabular form in terms of mean, standard deviation and percentages.

4.2 Nature, Forms and Types of Strategic Alliances

In this section, the study looks at the presence and forms of strategic alliances within the commercial banks. The section is concerned with highlighting the presence and forms of strategic alliances within the commercial banks. This involves linking the characteristics of the partners and their subsequent strategic motives. The relationship and resource characteristics have been linked to the strategic motives of the partners.
4.2.1 Existence of Strategic Alliances

The findings of the study reveal that all the commercial banks were involved in some form of strategic alliances. As can be seen from Figure 4.1, all the respondents indicated that their organizations had joined some strategic alliance.

Figure 4.1 Presence of a Strategic Alliance

Source: Research Findings

4.2.2 Number of Strategic Alliances

As indicated in Figure 4.2, the study findings reveal that most the commercial banks had 3 – 4 alliances with 44.4% of the banks falling in this category while 34.9% were in 5 – 6 strategic alliances and 18.6% were had one to two strategic alliances. Banks that had more than 6 strategic alliances were 2.3%. In essence, all the commercial banks were in at least one form of strategic alliance. Section 4.2.3 will highlight the nature and forms of the various forms of strategic alliances as entered into by the commercial banks.
4.2.3 Types of Strategic Alliance

In total, the study was able to list 147 different alliances entered into by the banks, giving an average of 3.42 (approximately 3) alliances per bank. Table 4.1 gives the types of alliance formed by the commercial banks.

Table 4.1 Types of Alliances Formed

<table>
<thead>
<tr>
<th>Type of Alliance</th>
<th>Frequency</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Joint ventures</td>
<td>2</td>
<td>1.4</td>
</tr>
<tr>
<td>Equity strategic alliance</td>
<td>45</td>
<td>30.6</td>
</tr>
<tr>
<td>Licensing Agreement</td>
<td>58</td>
<td>39.5</td>
</tr>
<tr>
<td>Contractual agreements</td>
<td>25</td>
<td>17.0</td>
</tr>
<tr>
<td>Distribution Agreement</td>
<td>9</td>
<td>6.1</td>
</tr>
<tr>
<td>Supply Contracting</td>
<td>8</td>
<td>5.4</td>
</tr>
<tr>
<td>Total</td>
<td>147</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Research Findings
Most of the strategic alliances (39.5%) involved entering into licensing agreement with partners while 30.6% were equity strategic alliances and 17.0% were outsourcing agreements. Distribution agreements were 6.1%, supply contracting 5.4% and joint venture were 1.4%.

Data gathered from the questionnaires reveals that the most common form of strategic alliance was that involving banks and money transfer operators (MTOs). Many of the banks had partnered with both local and international money transfer operators. Locally, Safaricom (M-Pesa) and Airtel (Airtel Money) had the most number of strategic alliances with commercial banks. Internationally, the MTO that had formed strategic alliances with banks included Western Union, MoneyGram, XpressMoney and Dahabshiil and American Express. Most of the local banks established alliances with foreign corresponding banks to cover international transfer corridors. By working with MTOs, the banks located in the local market could gain international correspondents banks and Society for Worldwide Interbank Financial Telecommunication (SWIFT) membership that allow them to offer remittance services abroad and cross-border settlement services.

Respondents revealed that most of the strategic alliances between commercial banks and MTOs were usually agreements determining how revenue was to be shared out between the two partners. This was due to the fact that most of them were transaction based where the banks and MTOs gained revenue depending on the size and number of transactions, and their inceptions was not capital intensive. Thus in most of these alliances there wasn’t a significant amount sent aside for the venture. Commercial bank operations are IT intensive. The study was able to learn that most of the commercial banks had entered
into sub-contracting partnerships with IT firms for the production, supply and maintenance of the bank’s core banking systems.

4.3 Performance Trend

The performance trend of commercial banks was determined through an analysis of the percentage change in profit before tax and total assets for commercial banks between 2009 – 2012. This finding has been captured in Figure 4.3. Commercial banks in Kenya recorded the highest percentage change in profit before tax and total assets in 2010; 58.2% and 26.3% respectively. In 2012 the percentage change in profit before tax was 34.1% while that of total assets was 17.3% and in 2011 it was 24.7% for profit before tax and 20.9% for total assets.

Figure 4.3 Annual % Change in the Performance of Commercial Banks

Source: Research Findings
The overall percentage change of profit before tax between 2009 and 2012 was 164.6% an indication that there was increased profitability within the banking sector within this period. The % change in total assets within the same period was 79.1% an indication of increased growth within the sector.

The study notes that with the emergence of mobile money transfer services in 2007 and its subsequent integration into the core banking services in the following years, the increased profitability in banks in 2010 could be partly attributed to this phenomenon. The most notable strategic alliances involving banks and mobile operators within 2009 – 2010 include Eazzy 24/7 and M-Benki.

The average mean of the return on assets of the commercial banks within 2009 – 2009 is given in table 4.2.

### Table 4.2 Mean on Return on Assets (2009 – 2012)

<table>
<thead>
<tr>
<th>YEAR</th>
<th>2012</th>
<th>2011</th>
<th>2010</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Av. Mean on Return on Assets</td>
<td>0.0404</td>
<td>0.0361</td>
<td>0.0363</td>
<td>0.0294</td>
</tr>
</tbody>
</table>

Source: Research Findings

### 4.4 Correlations Analysis

Correlation analysis was carried out to establish the relation between the study variables. This yielded a value of R is 0.747 which shows that a strong relationship between the study variables exists.

### Table 4.3 Correlation Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.724*</td>
<td>.612</td>
<td>.747</td>
<td>.68271</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), FINANCIAL LEVERAGE, BANK SIZE, PROPORTION OF FUNDS
b. Dependent Variable: Financial Performance (ROA)

Source: Research Findings
The correlation analysis presented in table 4.3 give the adjusted coefficient of determination $R^2$ as 0.747, showing that the variation of 74.7% exists in the performance of commercial banks as a result of ROA, financial leverage and bank size and proportion of funds set aside for strategic alliances. This numerical evidence is strong enough to support that there exists a strong relationship between the variables.

4.5 Pearson Correlation Coefficient Analysis

Table 4.4 indicates the Pearson Correlation Coefficient matrix between proportion of funds set aside for strategic alliances, the leverage, the bank size and the financial performance of commercial banks. The findings reveal that there is a strong positive relationship between performance of commercial banks, proportion of funds set aside for strategic alliances and bank size of magnitude 0.885 and 0.862 respectively. On the other hand, there existed a strong negative correlation between financial performance and financial leverage of magnitude 0.872. The strong positive correlation was found to be significant with a P value of 0.026 and 0.047 respectively. The negative correlation between firm performance and financial leverage had a P value of 0.034. There existed a positive correlation between bank size and the proportions of funds set aside for strategic alliances with a magnitude of 0.390. This positive correlation was found to be statistically significant with a P value of 0.03 which is less than 0.5.
Table 4.4 Pearson Correlation Coefficient Matrix

<table>
<thead>
<tr>
<th></th>
<th>Performance of Banks</th>
<th>Proportion of Funds in SA</th>
<th>Financial Leverage</th>
<th>Bank Size</th>
</tr>
</thead>
<tbody>
<tr>
<td>Performance of Banks</td>
<td>Pearson Correlation</td>
<td>1</td>
<td>.885*</td>
<td>-.872*</td>
</tr>
<tr>
<td></td>
<td>Significance</td>
<td>.026</td>
<td>.034</td>
<td>.047</td>
</tr>
<tr>
<td>Proportion of Funds in SA</td>
<td>Pearson Correlation</td>
<td>.885*</td>
<td>1</td>
<td>-.120</td>
</tr>
<tr>
<td></td>
<td>Significance</td>
<td>.026</td>
<td>.379</td>
<td>.003</td>
</tr>
<tr>
<td>Financial Leverage</td>
<td>Pearson Correlation</td>
<td>-.872*</td>
<td>-.120</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Significance</td>
<td>.034</td>
<td>.379</td>
<td></td>
</tr>
<tr>
<td>Bank Size</td>
<td>Pearson Correlation</td>
<td>.862*</td>
<td>.390**</td>
<td>.025</td>
</tr>
<tr>
<td></td>
<td>Significance</td>
<td>.047</td>
<td>.003</td>
<td>.853</td>
</tr>
</tbody>
</table>

Source: Research Findings

4.7 Multiple Regression Analysis

Multiple linear regression analysis was carried out using SPSS version 17.0. The analysis was used to determine the relationship between financial performance of the banks and the independent variables.

Table 4.5 Multiple Regression Coefficient

<table>
<thead>
<tr>
<th>Variables</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>3.691</td>
<td>1.014</td>
<td>3.401</td>
<td>0.003</td>
</tr>
<tr>
<td>Proportion of funds set aside for SA</td>
<td>1.182</td>
<td>.086</td>
<td>.580</td>
<td>2.085</td>
</tr>
<tr>
<td>Financial leverage</td>
<td>-1.149</td>
<td>.375</td>
<td>-.223</td>
<td>.854</td>
</tr>
<tr>
<td>Bank size</td>
<td>3.002</td>
<td>.093</td>
<td>1.014</td>
<td>1.023</td>
</tr>
</tbody>
</table>

Source: Research Findings

The resultant regression model is of the form:

\[ Y = 3.691 + 1.182PSA + 3.002SZ - 1.149\text{Lev} \]

Where

\[ Y \] = Financial Performance of banks measured by ROA

\[ PSA \] = Proportion funds set aside for Strategic alliances

\[ LEV \] = Leverage measured by debt/equity

\[ SZ \] = Size of the bank as measured by the natural log of the book values of the assets
The beta coefficients in the regression analysis in Table 4.5 explain the relative importance of the independent variables in contributing to the variance of the financial performance (the dependent variable). Thus bank size carried the heaviest weight (Beta = 1.014, significance = 0.41), followed by the proportion of funds set aside for strategic alliances (Beta = 0.580, significance 0.04) and then the financial leverage (Beta = -1.149, significance 0.039). According to these results, a positive change in the proportion of funds set aside for strategic alliances and bank size leads to a positive in change in the financial performance of commercial banks while a negative change in the financial leverage of the banks leads to an inverse change in the financial performance.

The study notes that all the independent variables, that is; the proportion of funds set aside for strategic alliances, bank size and financial leverage, are significant predictors of a bank’s financial performance at a 5% significance level. Proportion of funds set aside for mergers had significant predictor of performance (t = 2.085), size of bank (t = 1.023) and leverage measured by debt equity (t = 0.854). In essence, increasing the proportion of funds for strategic alliances and the size of bank and lowering of financial leverage is expected to improve the financial performance of a commercial bank.

4.8 Interpretation of the Findings

The purpose of this study was to establish the effect of strategic alliances on the financial performance of commercial banks in Kenya. Data collected from financial statements was keyed into SPSS and analysis made. The following regression model was used:

\[
Y = \beta_0 + \beta_1 \text{PSA} + \beta_2 \text{SZ} + \beta_3 \text{LEV} + \varepsilon
\]

- Y - Financial Performance of banks measured by ROA (net income/total assets)
- PSA - Proportion of funds that the bank has put in the Strategic Alliance
- LEV - Leverage measured by debt/equity
SZ - Size of the bank as measured by the natural log of the book values of the assets

$\beta_0, \beta_1, \beta_2, ..., \beta_N$ - Coefficients of Variations

The results of the regression analysis reveal that financial leverage is inversely related to financial performance meaning that as financial leverage increases by 1, profitability decreases by 1.149 and vice versa. Profitability is defined as the return earned on the total assets of a company. On the hand, proportion of funds and bank size are directly proportion to the profitability of the organization meaning that as the two increase so does the profitability of the company.

Nzengya (2013), in his study, Strategic Alliances Among Commercial Banks in Kenya, found out that some commercial banks are not involved in any strategic alliance as indicated in the table below.

**Table 4.6 Has your bank entered into a Strategic alliance?**

<table>
<thead>
<tr>
<th>Response</th>
<th>Frequency</th>
<th>Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>26</td>
<td>87</td>
</tr>
<tr>
<td>No</td>
<td>4</td>
<td>13</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Nzengya 2013

Table 4.6 shows that 26 (87%) had entered into strategic alliances while 4 (13%) had not. This indicates that majority of the banks surveyed had entered into some form of strategic alliance. Nzengya’s results contradicts with my this research’s findings since the findings of this research indicate that all banks were involved in at least one strategic alliance.
CHAPTER FIVE
SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction
The objective of the study was to investigate the effect of strategic alliances on the financial performance of commercial banks in Kenya. Of concern to the study was to determine the proportion of funds set aside for strategic alliances by commercial banks in Kenya and the resultant effect on profitability of the institutions. This gives a summary of the study and makes conclusion and recommendations based on the results. The chapter also presents implications from the findings and areas for further research.

5.2 Summary
These study revealed that commercial banks in Kenya have entered into various strategic alliances in order enhance the achievement of their strategic objectives. On average, the banks have at least three strategic alliances. Alliances with mobile transfer operators were cross cutting among the commercial banks. The statistical analysis of the data show that the proportion of funds set aside for strategic alliances, the financial leverage measured by debt/equity and the size of a bank have a bearing on the financial performance of the financial institutions.

On issue with diffusion of technology and improve customer service more than half of the respondents gave out the view that alliances really target to tackle the two issues so as to retain more customers at a cheaper cost. Also financial stability was to be realized if technology was invested and also operation cost was to be minimized thus a synergy to increased revenue for both companies. Brand reputation is a psychological element that every player in the market has to invest in.
On the other hand few loopholes have been identified in relation to that affect the alliance negatively. But the major problems is the system failure that need to give consistent and reliable data of all the transactions done under the alliance, thus its failure becomes a hindrance to convince the customers to use service offered by both organizations. The negative attitude that the customers may have really affects the loyalty that they have for the organizations. Different Key Performance Indicators and different financial year date reports also bring about disparity since the organizations do not run at the same lanes. Also as the organizations have different goals and objectives the uniformity of the operation under the alliance also gets affected since they aim at achieving different goals.

5.3 Conclusion

The study concludes that other factors held constant the increased presence of strategic alliances within the banking sector has greatly contributed to the profitability of commercial banks in Kenya. The highest change in pre-tax profit and increase in total assets among the commercial was recorded in 2010. While there was 58.2% change in pre-tax profit, the experienced change in total assets was 26.3%. between 2009 and 2012, commercial banks experienced an average of 164.6% change in pre-tax profit and a % change in total assets of 79.1%. An R value of 0.747 is an indication that there exist a strong relationship between the proportion of funds set aside for strategic alliances, financial leverage and size of banks with financial performance of commercial banks. A strong positive correlation between performance of commercial banks, proportion of funds set aside for strategic alliances and bank size exist with a magnitude 0.885 and 0.862 respectively. There exist a strong negative correlation between financial performance and financial leverage of magnitude 0.872.
5.4 Policy Recommendations

The findings of this study has revealed that proportion of funds set aside for mergers, the financial leverage of banks measured by debt/equity and the bank size have a bearing on their financial performance. In essence, this variables influence the profitability of commercial banks. Therefore, it is important not only for commercial banks but also for other organizations to factor in these variables while looking at ways of increasing their profitability. The findings further recommends that commercial banks should always strive to ensure that they increase the number of strategic alliances while at the same time ensuring that their financial leverage is kept as low as possible.

The study also established that most commercial banks were willing to enter into such arrangements in order to get various benefits. However due to a number of challenges encountered the gains were not maximized. It is therefore necessary for those banks already in a strategic alliance to deal with the challenges in order to realize even more gains. Careful choice of the strategic partners is also important so as to avoid conflicts of any sort. This will also ensure a sustainable relationship where the partners can complement each other in more synergistic manner. The reduction of competition was cited as one of the drivers of alliances. This may build monopolies in the industry which could face a lot of government control and reduce the gains.

5.5 Limitations of the Study

The focus of this study was only commercial banks while the financial statements used were for the period 2009 – 2012 and therefore cannot be generalized for all financial institutions in Kenya. The study relied on both primary and secondary data of which the secondary data was collected from financial statements of the commercial banks.
Although there are general guiding principles for the preparations and reporting of the financial statements which are Generally Accepted Accounting Principles and International Financial Reporting Standard, the study realized that the statements were not in the same format, with the banks using different accounting policies. Therefore the reliability and quality of this data cannot be considered to be 100% perfect. Whereas a collection of data for a longer period would have been more appropriate, collection of such data was not possible.

Since the main purpose of this study was to determine the effect of strategic alliances on the financial performance of commercial banks in Kenya, Central bank considered some information sensitive and confidential and thus the researcher had to convince them that the purpose of information is for academic research only and may not be used for any other intentions.

The findings of this study may not also be generalized to all commercial banks across the globe but can be used as a reference to commercial banks in developing countries since they face almost the same challenges due to the same prevailing economic situations as opposed to commercial banks in developed countries.

5.6 Suggestions for Further Research

This study finds the need for similar studies to be carried out targeting other financial institutions and should incorporate more financial parameters. At the same time, there is need for further research targeting narrowing down on how each type of strategic alliance entered into by financial institutions contribute to the financial performance of the organization. Specifically, such studies should analyze each strategic alliance (mergers
and acquisitions, joint ventures, outsourcing, affiliate marketing, franchising and product licensing) outside the umbrella of strategic alliances.

Despite the limitations of this study, scholars should be able to utilize these findings to create novel studies for further investigations on other key issues relating to strategic alliances in the banking industry. Studies could also be conducted in other industries other than banking in order to validate or invalidate the findings of this study. The study findings are according to the firms’ management point of view. The scope of the study may also be extended to cover the views of other key stakeholders in the banking industry such as the Central bank of Kenya and the Mergers and Monopolies regulation authority.

The study looked at the factors that led to the strategic alliances in commercial banks and also the challenges that face the alliances. The results showed that the strategic alliance really helps an organization to have a competitive advantage than those ones that go alone. There is need therefore for more study to be done how the organization need to be prepared if an alliance breaks up and what will be strategies that the organization will take to sustain itself after the break up.
REFERENCES


APPENDICES

APPENDIX I: Data Collection Form

I am Nancy Chepkorir Kilimo, a postgraduate student at the University of Nairobi. As part of the requirements for the degree of Master of Science in Finance, I have to undertake a research study. This study seeks to determine the effects of strategic alliances on the financial performance of commercial banks in Kenya. All the information provided will be confidential and will be used for academic purpose only. Your contribution towards this research will be very important and much appreciated. I assure you that I have obtained the necessary authorization and consent to carry out this study.

1. Name of the Bank

2. Is the bank involved in any Strategic Alliance(s)? (tick)
   a) Yes ☐  b) No ☐

3. If yes, how many Alliance(s)?

4. Kindly list the Alliance(s)

5. How much has the bank set aside for each Alliance(s)?

Thank you for your time.
APPENDIX II

LIST OF COMMERCIAL BANKS IN KENYA AS AT 31ST DECEMBER 2013

1. ABC Bank (Kenya)
2. Bank of Africa
3. Bank of Baroda
4. Bank of India
5. Barclays Bank Kenya
6. CfC Stanbic Holdings
7. Chase Bank Kenya
8. Citibank
9. Commercial Bank of Africa
10. Consolidated Bank of Kenya
11. Cooperative Bank of Kenya
12. Credit Bank
14. Diamond Trust Bank
15. Dubai Bank Kenya
16. Ecobank Kenya
17. Equatorial Commercial Bank
18. Equity Bank
19. Family Bank
20. Fidelity Commercial Bank Limited
21. First Community Bank
22. Giro Commercial Bank
23. Guaranty Trust Bank Kenya
24. Guardian Bank
25. Gulf African Bank
26. Habib Bank
27. Habib Bank AG Zurich
28. Housing Finance Company of Kenya
29. I&M Bank
30. Imperial Bank Kenya
31. Jamii Bora Bank
32. Kenya Commercial Bank
33. K-Rep Bank
34. Middle East Bank Kenya
35. National Bank of Kenya
36. NIC Bank
37. Oriental Commercial Bank
38. Paramount Universal Bank
39. Prime Bank (Kenya)
40. Standard Chartered Kenya

41. Trans National Bank Kenya
42. United Bank for Africa
43. Victoria Commercial Bank

Source: Central Bank of Kenya