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The Effect of Credit Cards on the Competitiveness of Commercial Banks in Kenya (A Survey of Commercial Banks in Meru County)

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Abstract: This research sought to find out the effect of credit cards services on the competitiveness of commercial banks in Kenya. The objectives were to determine the effect of credit cards services on the competitiveness of commercial banks. The theories used to underpin the study were, traditional theory of financial innovations, financial constraints theory and strategic theory of financial innovations. A descriptive research design was adopted in conducting this study. The target population was 239 upper and middle cadre employees of the commercial banks. Stratified proportionate sampling technique was used by taking 11 branch managers 32 heads of departments, 25 agency banking operators and 82 management staffs from commercial banks in Meru town. This resulted in a total sample size of 150 respondents. Primary data was collected using open and close ended questionnaire. Secondary data was collected from banks websites, central banks websites and various publications. Descriptive statistics was used to analyze the data. Binary logistic regression was used to link the relationship between independent variables and dependent variable and to test the hypothesis. The researcher used the hypothesis test at 95% confidence level. Descriptive data was presented in the form of frequency tables and percentages. The data was analyzed using SPSS. The study concludes that mobile virtual network had a positive relationship on competitiveness of commercial banks.. The study recommends that the regulator (Central Bank of Kenya) should create an enabling environment that will enhance competitiveness of commercial banks so that they realize the full benefits of value added services. Through compliance with the regulations and policies the banks will be more competitive as a result of value added services innovations which without a proper policy the banks would not operate effectively in the market to realize profits.

Keywords: Competitiveness, value added services, customer service, information technology and credit cards.

1. Introduction

Globally, the performance of a firm is influenced by the level of competition. A strategic plan is essential in making a firm to be at a more competitive advantage than others (Silber 1983).The number of competitive strategies is as much as there are many competitors. In order to remain competitive commercial banks have introduced various ways of offering financial services to its clients. Rapid structural changes and adoption of various value added services has changed the international financial system (Suzuki, 2006). The increased efficiency of international financial markets due to value added services has made banks to be more competitive by offering a wide range of services

In addition, most firms in Africa started as small and medium enterprises and grew through the five stages to big financial institutions with advanced technology. As competition intensified those firms that were able to challenge the competition in the market strived and they changed in complexity of product and service they offer in the market and also grew in size. Development in information technology by commercial banks has served to improve competitiveness, streamline methods of operation, and it has brought revolution in the functioning of the banks. Competition is the main strategy of a firm to ensure growth stability and survival

Further in Kenya, commercial banks operates in an economic environment where restrictions in law and systems are lessened with the presence of both local and multinational banks such as diamond trust bank, Barclays bank of Kenya, Standard chartered bank among others. These banks have similar segmentations of their banking business into key divisions like corporate business banking which takes care of the large corporate banking requirements and personal business banking that takes care of banking needs of individuals. Hence the operating environment is very competitive where most banks have gone to extent of participating in road shows and even hawking their services by the road side. The critical issues affecting the banks are finding new ways that will enable them to be at a more competitive edge than their counterparts in the industry, low levels of customer service and how to reduce operation costs.

For example Value added services such as mobile virtual networks by Equity bank's Equitel and Commercial bank of Africa's mshwari banking technology among others have redefined how funds transfers were done traditionally through banks as they try to compete with each other. These issues can be attributed to its policies and the procedures of acquisition of its services by their clients. Value added services are often associated with the strengthening the status of many economies. it is quite clear that value addition of services affects not only banking services but also how the economy of a nation develops and its ability to achieve continued growth. Value addition of services has enabled ease of access, processing, storage, transfer and delivery of services and products.(Njuguna, 2011).

Furthermore, value addition of services in banking institutions saves time, makes inquiry easy and contributes to service delivery improvement. in recent years information technology investment by banking institutions has smoothened operations, improved service delivery and increased competitiveness. it has led to revolution of the way banks function. it is argued that financial services industry has experienced great structural changes because of the revolution of the internet. Banks are widely involved in better information technology based services and also in management of their products pricing and management of risks. This has been facilitated by huge investment in technology to maintain and upgrade their infrastructure. New off the shelf information technology services like mobile banking has enabled commercial banks to utilize the advancement in technology at very low costs. These developments have ultimately changed the competitive environment of commercial banks in Kenya (Francesca, 2010

Commercial banking started in Kenya in the beginning of the 20th century with the partitioning of Africa by the European colonial powers. National bank of India was the first to start a branch in Mombasa in 1986.By the turn of 1972, 12 commercial banks had already started operations in Kenyan market. The Kenya banking sector comprises mostly of local and several foreign players in the industry like standard chartered bank, diamond trust bank and Barclays bank of Kenya. The key divisions in most banks are personnel banking for individual needs and corporate business banking for large companies banking requirements. The banking operative environment is very competitive as these banks fight for sizeable share of the market. The various constraints facing the banks include reduction in costs and new value added services innovation that enables them to be at a competitive edge. Other issues are huge and costly working management staff, inefficient customer service and occasional cases of forgery and frauds. These issues are attributed to work bureaucracy in provision of banking services including credit facilities. The innovations of mobile money transfer technologies like Mpesa, Telcomcash and Mswari amongst others have revolutionized from former over the counter funds processing and transfer. Automated payments like credit cards have replaced full service branches. Again corporate banking transactions are affected in such a way that physical presence in a given market center is not required.

1.1 objectives
1.1.1 Main objective
The general objective of the study was to determine the effect of credit cards services on the competitiveness of commercial banks in Kenya

1.1.2 Specific objectives
- Determine effects of customer royalty on banks competitiveness
- Identify effects of convenience of credit cards on banks competitiveness
- To highlight the importance of customers' time saving on banks competitiveness
- Importance of credit cards user friendliness on banks competitiveness

1.1.3 The scope of the study
The study was carried out in Meru County. It was only based on the registered commercial banks.

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2. Literature Review

2.1 Theoretical review
2.1.1 Strategic Theory of Financial Innovation.
Sundbo (1997) emphasized that core determinant of the value added services innovation should be firms strategy. Consequently, value added services innovation is formulated within the firm's strategy and must be kept within the firm's strategy to prevent firm's activities from deviating from its goals and objectives. These often involve deliberate financial engineering, where innovation is systematically planned and strategically operationalized to improve performance of specific sections.

Tufano (1989) emphasized that value added services innovation makes the financial market complete, wide and efficient. This reduces the cost of transactions and gives the participants greater freedom of investment of choice thereby satisfying all the participants in the finance industry.

Merton (1992) holds that the period from mid-1960s to mid-1980s shows that value added services innovation has been a critical persistent part of the economic landscape of the world financial markets. He holds that financial markets have continued to produce a multitude of new products, including many new forms of derivatives, alternate risk transfer products, and exchange traded funds. In his view we see companies today coming up with new products that are less costly and friendlier to customers as they are designed to meet the dynamic environment which they operate and thus this strategy enhances their competitiveness in the market.

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2.1.2 Empirical review
According to Naim (1995), a credit card is a card issued by commercial banks granting the holder an option to borrow funds. Credit cards attract interest and are basically used for short term financing. Interest starts accumulating one month after a purchase is made, and borrowing levels pre-set according to the holder's rating. A bank which is issuing credit cards has to manage every aspect of the lending process in order to be competitive because of strong competition from other issuers, including nonbanks.

According to (Phil, 2011), he found out that in addition to traditional consumers, other groups of consumers such as university students and disabled customers have adopted the use of credit cards to acquire various products and services due to advancement in technology and internet. University students are now finding themselves in situations whereby they are obliged to make decisions impacting on their financial independence. This is due to growing responsibilities that affect their financial security and future well-being. This trend has received great attention from both the government and financial institutions. The role of the financial institutions including banks is to promote the well-being of the society by controlling consumptions and investment decision. The commercial banks has tapped into this market by making the students' access credit by use of credit cards. This has influenced the students' lifestyle and purchasing power.

According to Weistart (1972), he found out that credit cards have been used as a means of facilitating delayed payments purchased since early in the century. The first credit card systems were operated by service organizations and retailers in connection with the merchandising of their products. While such programs were used in local markets by departmental stores, oil companies were the first issuers to recognize the potential of credit card plans in the larger geographical areas. The efforts of the new, independent issuers were concentrated upon the solicitation of accounts, the evaluation of cardholder credit standing and the development of centralized accounting and the processing systems. Since these services are closely related to services provided by the traditional financial institutions, it is not surprising that banks 17 undertook to create their own credit card systems Commercial bank charge cards are being used by more American consumers in their purchasing behavior than ever before. The number of the users of the bank credit card is steadily on the increase and has become an area of consumer behavior that has received recent attention in the marketing literature. Recently, the financial institutions have realized that in order reach new market share, provision of credit services is inevitable. This is because provision of credit has increasingly facilitated acquisition of goods and services.

According to Mathews and John (1969), they found out that despite the worst recession in recent years, there are some signs of economic growth influencing the use of credit cards as customers lower their spending. Credit cards usage means that consumers have an obligation to pay out their debts from their future earnings. Therefore it is hard for them to see debt as a good thing .But credit cards have a good impact on the growth of the economy. This is because consumer purchase goods and services they couldn't afford. By making those purchases, businesses are able to generate income they may not have were it not for credit lines extended to consumers. This has an effect of stimulating the economy in the long run.

According to Robb& Sharpe (2009), he found out that many international customers have realized that life was made easier by being able to pay for their goods and services by use of plastic cards. This makes it convenient for consumers since they don't have to carry cash in their destination country currencies. Visas and master cards are the two largest card associations widely used throughout the world to effect payments.

According to Steve (1995), he found out that credit cards usage has turned into prosperous business. This is as a result of income from fees associated with the use of credit cards. Therefore credit cards have been widely accepted worldwide as a means of acquiring goods and services. Small business deal with liquidity problems using business credit cards. This makes it easier for business to expand. By accessing the required funds the small business may end up being a big business with more employees in the long run. He found out that firms with business credit cards grow at a faster rate than the ones without them. Again due to advancement of management information technology, there has been a decline in liquidity limitations faced by 18 prospective business people. This is because credit lines have become widely available due to advanced risk scoring procedures that banks use to diversify their risks. This makes it easier for business to acquire a loan.

According to Douglas (2005), he found out that theoretically credit card usage is expected to have a positive effect on the financial performance of the commercial banks, as the credit card results in more income from the interest charged to the customers and the interchange fees that the merchants pay to the banks. In addition, the late payment charges, the annual charges, charges for printing a statement, charges for issuing a new card and the renewal fees.

Studies done by Lawrence M Ausubel (1991) concluded that during 1980's, bank credit card operations earned 3-5 times the rate of return earned in the banking industry at large. The credit card market dynamics in recent years have made commercial banks to be very cautious on all aspects of lending process. This is because despite the success of earlier years, today's competition as a result of advancement in technology should be properly managed in order to realize more profits. Various market dynamics have made credit cards to be one of the most competitive areas in the industry. Therefore proper risk management systems and operating policies should be tied to the firm's business goals and plans.

According to Cohen (2005), he found out that factors like revenue generation and customer satisfaction influence performance of credit cards portfolio .Purchase done through credit card affects the economy compared with individual savings especially in emerging economies. The customers expect the bank to deliver quality services and products. They also expect to use the credit cards wisely .Therefore if the bank fails to disclose full information on credit cards ,the customers' expectations will not be delivered making them dissatisfied. The customers do not expect to be held responsible for any unjustified charges or any fraudulent activities done without their knowledge. Therefore it is important for the card issuers to communicate well on the quality of services they are able to provide. This will enable the card holder to be royal as a result of satisfaction achieved by getting the products and services they expect from the bank. This will have a direct impact on the increase of customer base leading to increase in revenue generation by the bank.

According to Nash (1993), he found out that since 1970's there has been growing evidence supporting the frequently heard conjecture that credit cards encourage spending. Credit cards business gives more returns in terms of profits than other banks business products. For example it is known that people who own more credit cards make larger purchases. There is also evidence that credit card users are more likely to underestimate or forget the record on their purchases.

Studies done by Mathews and Slocum (1969) found the upper classes are generally favorable toward using credit to purchase luxury goods and the lower class users tended to use their for durable and necessity goods. There exists a number of interesting and useful relationships between social class and income and the usage of bank credit cards. For instance, they found out that members of the lower social classes tend to use their cards for installment purposes and upper classes for convenience. Further their results indicated that all the users had a favorable general attitude toward credit; however, installment users tended to use their cards more frequently.

Mutua (2010) found out that there are some success factors that are useful in influencing customer desire to use bank services. Some of these are technological, human resource, finance and service delivery quality. He carried out the research on commercial banks in order to determine the relationship between key success factors and bank strategy in the credit card sector. Key success factors are those things that enable or increases the ability of industry players to be more competitive in the market. The banks should be very competent and pay lot of concentration on the success factors in order to be at a competitive edge. The success factors are directly related to achievement of higher profits and income of the commercial banks. Since the key success factors are dynamic in nature and vary from time to time. The bank managers should constantly identify the ones that are most important to the future competitiveness of the bank. Again they should do away with the ones that have little impact to the going concern of the bank.

Makio (2010) found out that the majority of staff in post bank holding credit cards were top management contrary to the middle and lower level management who had none. He also found out that some of the reasons for failure to possess credit cards were lack of awareness and fear of fraud. He found out that even though there are benefits of credit cards such as convenience and security from theft of cash, there is low uptake of credit cards by lower and middle level of 23 management. This implies that the level of income and the amount of money passing in the hands of these lower level of management has an effect on the ownership of credit cards. The top management has an incentive of higher incomes and are more likely to have the ability to fulfil the obligation associated with credit cards of repaying the interest and commissions attached to them

3. Methodology

3.1 Study design

The research design employed descriptive survey research design. Quantitative data was collected and measured in terms of figures to describe perceptions of respondents. Detailed information was obtained in order to come to useful conclusion in this study.

3.1.2 Target population

The target population of the study was the 17 registered commercial banks in Meru County. Accessible population was 239 and comprises of 17 branch managers, 51 head of operations, treasury and risk management departments, 40 Agency banking operators and 131 management staff.

3.1.3 Sample and sampling procedure

The sample size was determined by using Slovin's sample size formula=N/ (1+N (e) 2).Stratified proportionate sampling technique was used by taking 11 branch managers 32 heads of departments, 25 agency banking operators and 82 management staffs from commercial banks in Meru town. This resulted in a total sample size of 150 respondents.

3.1.4 Data analysis

Data was coded to facilitate analysis. It was analyzed with aid of IBM statistical software. Binary logistic regression model was used. Data was categorized and arranged to determine how independent and dependent variables related.

3.1.5 Research findings

According to a research we conducted on effect of cheques truncating systems on competitiveness of commercial banks, the computed significance level P – value=0.615> 0.05. Hence, we fail to reject the null hypothesis and conclude that there is no significant relationship between credit cards services and competitiveness of commercial banks in Kenya.

3.1.6 Conclusions

Based on the finding we draw the following conclusions.

There is no significant relationship between credit cards and competitiveness of commercial banks in Kenya. This contradicts the study by Kyalo (2014) who established that credit card usage is expected to have a positive effect on the competitiveness of the commercial banks, as the credit card results in more income from the interchange fees that the merchants pay to the banks and the interest charged to the customers including, the late payment charges, charges for printing a statement, the renewal fees, charges for issuing a new card and the annual charges. The study is in agreement with Matiru (2007) who found out that customers have not well embraced the use of credit cards because they fear liability of debt since they avoid risk and others fear possibility of any fraudulent activity.

3.1.7 Recommendations

The study recommends that the regulator (Central Bank of Kenya) should create an enabling environment that will enhance competitiveness of commercial banks so that they realize the full benefits of value added services. Through compliance with the regulations and policies the banks will be more competitive as a result of value added services innovations which without a proper policy the banks would not operate effectively in the market to realize profits.

From the findings and conclusions in this chapter, the study recommended that for all the commercial banks to earn more profit, increase number of customers, for their business to grow further and also for them to invest more they should embrace the adoption of value added services.

The study also recommends that the firms also should ensure that they adapt the new value added services innovation in order to cope with the fast changing technology. Value added services encourages ease of flow of information and fast delivery to the intended persons.

The study also recommends that, for efficient adoption of value added services, there should be reliable infrastructure, enough financial resources; and the staff should be equipped with adequate skills and knowledge on the new technology through regular training in order to ensure that they do not resist the adoption of the new technology in the bank.

The value added services can be effectively adopted if there are quality systems in place, there is good information flow, there is specialization and also if the management fully supports the competitive strategies. The power of value added services innovation in helping commercial banks retain and grow competitive position is indisputable.

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