ASSESSMENT OF INTEREST RATE CAPPING ON COMMERCIAL BANKS IN KENYA

BY

GODFREY MUTINDA PETER

UNITED STATES INTERNATIONAL UNIVERSITY - AFRICA

SUMMER 2018
ASSESSMENT OF INTEREST RATE CAPPING ON COMMERCIAL BANKS IN KENYA

BY
GODFREY MUTINDA PETER

This Research Project Report is submitted to the Chandaria School of Business in Partial Fulfilment of the Requirement for the Award of the Degree of Masters in Business Administration (MBA)

UNITED STATES INTERNATIONAL UNIVERSITY - AFRICA

SUMMER 2018
STUDENTS’ DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University - Africa in Nairobi for academic credit.

Signed: ______________________   Date: ______________________
Godfrey Mutinda Peter (ID No: 655441)

This research project report has been presented for examination with my approval as the appointed supervisor.

Signed: ______________________   Date: ______________________
Dr. Peter Kiriri

Signed: ______________________   Date: ______________________
Dean, Chandaria School of Business
COPYRIGHT
Copyright © Godfrey Mutinda Peter, 2018

All rights reserved; no part of this work may be reproduced, stored in a retrieval system, transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise without the express written authorization from the writer.
ABSTRACT
The general objective of this study was to assess interest rate capping on commercial banks in Kenya. The specific objectives sought to determine the effect of interest rate capping of the competitiveness of banks in Kenya, assess the challenges posed to commercial banks by interest rate capping regulation, and to determine the strategies employed by commercial banks during interest rate capping.

The study adopted a cross-sectional survey design. This design method was selected on the basis that it can collect diverse information types and is quick and less costly. The population of interest this research study comprised of top and middle marketing managers from tier 1 Commercial Banks within Nairobi County who were 240. The sampling frame of the study consisted of the list of branch managers and was obtained from the Central Bank report. The sampling embraced a mixed method approach to sampling techniques involving stratified sampling technique and simple random sampling (SRS). The sample size was determined using the Yamane formula which gave the study a sample size of 68 managers. This study applied questionnaires collected from respondents as primary data which was analyzed quantitatively. The data was analyzed using descriptive statistics and inferential statistics. These were presented using tables and figures.

The study showed that interest rate capping has reduced bank profits and increased risk and operational cost for commercial banks. Interest rate capping has also increased access to finance to small corporations at the same time, it has reduced supply of credit. The study revealed that interest rate capping has led to development of new products or services in Kenyan commercial banks, and it has placed a strong emphasis on the development of new organizational processes, policies, products, and services.

The study revealed that interest rate capping has reduced profit margins and lending for Kenyan commercial banks. This has led to an increase in employee layoffs as well as heightening the operational cost and risk. The study showed that interest rate capping has not increased the expansion rate of commercial banks in Kenya, but instream, it has increased the evolving customer needs and the compliance of commercial banks with regulatory requirements since capping has rendered some processes obsolete.
The study indicated that the development of new products or services has improved the banks’ competitiveness in the Kenyan market and the fact that banks are offering different products to different demographic groups has led to new markets for the banks. Interest capping has increased the operational efficiency through system upgrades which has ultimately improved service delivery of commercial banks. The study showed that servicing a targeted market has ensured customer satisfaction and the introduction of many new processes, policies, products, and services has improved efficiency.

The study concludes that interest rate capping has not increased the level of performance of banks because it has increased financial risk of these banks. It has in fact increased the total cost of loans through additional fees which has led to an increase in probability of mergers and consolidation for bank survival. The study concludes that cost leadership strategy can be employed by banks to reduce operational cost, and enhance customer care to improve the relationship between commercial banks and clients.

The study recommends arrangement creators in this manner should re-examine the impact of the interest rate capping law and consider letting the market structure and credit risk play a major role. This is on account of banks fixing the loaning criteria given that they were not any more ready to remunerate danger of default by differing advance evaluating to coordinate the hazard accepted starting with one credit ask for them onto the next.
ACKNOWLEDGEMENT

My sincere gratitude and appreciation to my supervisor, Dr. Peter Kiriri, for his invaluable guidance patience and support during the research process and the preparation of this report.

Special thanks and appreciation to all my MBA lecturers from the year 2017-2018.
DEDICATION

I dedicate this research project report to my family
# TABLE OF CONTENTS

STUDENTS’ DECLARATION ........................................................................................................... ii
COPYRIGHT ................................................................................................................................. iii
ABSTRACT ................................................................................................................................. iv
ACKNOWLEDGEMENT ............................................................................................................... vi
DEDICATION ............................................................................................................................. vii
LIST OF FIGURES ...................................................................................................................... x
LIST OF TABLES ......................................................................................................................... xi
LIST OF ACRONYMS .................................................................................................................. xii

CHAPTER ONE .......................................................................................................................... 1
1.0 INTRODUCTION .................................................................................................................. 1
1.1 Background of the Study ..................................................................................................... 1
1.2 Statement of the Problem ................................................................................................... 5
1.3 General Objective .............................................................................................................. 6
1.4 Specific Objectives ............................................................................................................ 6
1.5 Significance of the Study ................................................................................................... 6
1.6 Scope of the Study ............................................................................................................. 7
1.7 Definition of Terms ........................................................................................................... 8
1.8 Chapter Summary .............................................................................................................. 8

CHAPTER TWO .......................................................................................................................... 10
2.0 LITERATURE REVIEW ....................................................................................................... 10
2.1 Introduction ....................................................................................................................... 10
2.2 Effect of Interest Rate Capping on Commercial Banks .................................................. 10
2.3 Challenges of Interest Capping on Commercial Banks .................................................. 14
2.4 Strategies Used by Commercial Banks during Interest Rate Capping ......................... 18
2.5 Chapter Summary .............................................................................................................. 22
LIST OF FIGURES

Figure 4.1: Gender ................................................................. 29
Figure 4.2: Age ...................................................................... 30
Figure 4.3: Job Level ............................................................. 30
Figure 4.4: Years in the Organization ..................................... 31
Figure 4.5: Size of Bank based on Capital Base ....................... 31
Figure 4.6: Number of Employees ........................................... 32
LIST OF TABLES

Table 3.1: Population Distribution ........................................................................................................... 24
Table 3.2: Sample Size Distribution ........................................................................................................ 26
Table 4.1: Rating of the Effect of Interest Rate Capping on Banks .......................................................... 33
Table 4.2: Correlations for Effect of Interest Rate Capping on Banks .................................................... 34
Table 4.3: Model Summary for Effect of Interest Rate Capping on Banks ............................................. 35
Table 4.4: Regression Coefficient for Effect of Interest Rate Capping on Banks ......................... 35
Table 4.5: Rating of the Challenges of Interest Rate Capping on Banks ............................................. 36
Table 4.6: Correlations for the Challenges of Interest Rate Capping on Banks ................................. 37
Table 4.7: Model Summary for Challenges of Interest Rate Capping on Banks ............................... 38
Table 4.8: Regression Coefficient for Challenges of Interest Rate Capping on Banks .................... 38
Table 4.9: Rating of the Strategies Used by Banks during Interest Rate Capping ............................... 39
Table 4.10: Correlations for Strategies Used by Banks during Interest Rate Capping ...................... 40
Table 4.11: Model Summary for Strategies Used by Banks during Interest Rate Capping .................. 40
Table 4.12: Regression Coefficient for Strategies Used by Banks during Interest Rate Capping ............ 41
LIST OF ACRONYMS

BOZ: Bank of Zambia
CBK: Central Bank of Kenya
CBR: Central Bank Rate
CDs: Certificates of Deposit
CIRP: Covered Interest Rate Parity
EAC: East African Community
ECB: European Central Bank
ICDC: Industrial and business Development Corporation
KBA: Kenya Bankers Association
KCB: Kenya Commercial Bank
M&A: Mergers and Acquisitions
MFIs: Monetary Financial Institutions
MPC: Monetary Policy Committee
NBFI: Non-Bank Financial Institutions
NPLs: Non-Performing Loans
NSE: National Securities Exchange
PMI: Purchasing Managers’ Index
SCP: Structure Conduct Performance
SMEs: Small and Medium Enterprises
SPSS: Statistical Package for the Social Sciences
SRS: Simple Random Sampling
UCIRP: Uncovered Interest Rate Parity
UK: United Kingdom
US: United States
CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Study
The recent introduction of lending rate caps for banks and other financial institutions has reopened an old debate over the appropriateness of regulatory intervention to limit the charging of rates that are deemed, by policymakers, to be excessively high (Maimbo & Gallegos, 2014). Move to cap commercial banks’ interest rates have changed the business environment forcing the financial institutions to align their operations to the changed environment (Xinhua, 2017). The general idea is that interest rate ceilings limit the tendency of some financial service providers to increase their interest yields especially in markets with a combination of no transparency, limited disclosure requirements and low levels of financial literacy (Maimbo & Gallegos, 2014). Capping of interest rates has a tendency to distort the market and cause adverse biases, which in turn leads to inefficiencies in the financial intermediation process (Ramsey, 2013).

Interest rates capping has been one of the common forms of government financial control that is widely used in both developed and developing countries. Several political and economic reasons motivate the use of interest rate caps, for example, to support a specific industry or sector of the economy where a market failure exists or where a greater concentration of financial resources is needed (Maimbo & Gallegos, 2014). Those market failures result from information asymmetries and the inability of financial institutions to differentiate between risky and safe clients, from adverse selection, and from moral hazard. Thus interest rate caps may be a useful mechanism for providing short-term credit to a strategic industry or for supporting a sector until it is sustainable by itself (Miller, 2013).

It is also often argued that interest rate ceilings can be justified on the basis that financial institutions are making excessive profits by charging exorbitant interest rates to clients. In implementing a cap, government is aiming to incentivize lenders to push out the supply curve and increase access to credit while bringing down lending rates. However, such thinking ignores the actions of the banks operating under asymmetric information. The imposition of a maximum price of loans magnifies the problem of adverse selection as the consumer surplus that it creates is a larger pool of willing borrowers with unidentifiable creditworthiness. Faced with this problem, lenders have three options: increase lending,
which will mean lending to more bad clients and pushing up Non-Performing Loans (NPLs); increase investment in processing systems in order to better identify good clients, which will increase overheads; increase investment in outreach to clients that can be identified as having good repayment potential, which will increase overheads. All of these options will increase costs and force the supply curve back to the left, which is detrimental to financial outreach (quantity of credit falls) (Miller, 2013).

Moreover, banks essentially make money from the difference between the rate which they pay depositors and the rate which they charge borrowers. These rates are determined by market forces, that is, demand and supply, but also several other factors come into play. And in this regard, commercial banks felt that placing a cap on interest rates would have an effect on the industry’s efficiency as it does not account for several factors such as market factors, that might affect the banks’ decision to opt for certain spreads (Honda & Kuroki, 2014). The major argument used against the capping of interest rates is that they distort the market and prevent financial institutions from offering loan products to those at the lower end of the market that have no alternative access to credit (Agolla, 2016). Many countries in Africa have established interest rate ceilings to protect consumers from high interest rates charged by lenders. Such ceilings are often the response of governments facing political or cultural pressure to keep interest rates low (Mbengue, 2013).

Many countries in both the developed and developing world have interest rate ceilings on consumer credit. These include France, Belgium, Netherlands, Poland, Slovakia, Ireland, some Australian states, Canada, some US states, Brazil, South Africa and Japan (Maimbo, Henriquez & Claudia, 2014). The German Supreme Court established an effective ceiling through its interpretation of its civil codes. In addition, Islamic banking prohibits the taking of interest and uses a profit-sharing mode. The primary objective of interest rate capping is to protect those of modest or low income from paying excessively high prices for credit. These ceilings often include both consumer and business borrowers in the scope of their protection (Honda & Kuroki, 2014). In France, interest rate ceilings differ depending on the type and length of loan: they are established at one third above the prevailing market rate for the particular market segment. South Africa has adopted a similar approach, with loans divided into seven categories. In Germany, the Supreme Court has established a very strong presumption that interest rates that are double the
relevant market rate are contrary to good morals. In contrast, the UK has not had general interest rate ceilings on credit since 1854 when Parliament, following Jeremy Bentham's strictures against usury, abolished the usury laws Japan (Maimbo et al., 2014).

Many countries in Africa have established interest rate ceilings to protect consumers from high interest rates charged by micro lenders. By 2013, 17 countries in Sub Saharan Africa had introduced interest rate caps (Djibril, 2013). Such ceilings are often the response of governments facing political or cultural pressure to keep interest rates low. In January 2013, Bank of Zambia (BOZ) introduced ceilings on the annual effective interest rate of loans charged by non-bank financial institutions (NBFI) (Djibril, 2013). The main reasoning for this offered by BOZ is that some NBFI were charging their clients excessive interest rates. The measures taken are supposed to make loans more affordable and equitable to vulnerable borrowers. In 2013, the West Africa Economic and Monetary Union, which includes eight francophone African countries, lowered the interest rate ceiling, initially established in 1997, by three percent (Djibril, 2013). The Economic and Monetary Community of Central Africa, comprised of 6 countries (Cameroon, the Central African Republic, Chad, the Republic of Congo, Gabon, and Equatorial Guinea), set up an interest rate ceiling in October 2012. The interest rate ceiling specific to the microfinance sector is calculated by applying a margin of 33% to the average effective interest rate charged by microfinance institutions during the previous six months (Djibril, 2013).

The last decade has been a period of dramatic changes for the banking sector in Kenya. Interest charged to borrowers rose to nearly thirty percent in the previous years. This generated a debate in parliament that resulted in interest rate capping. The capping of interest rates was on the table in 2012, but eventually Kenyan authorities abandoned the idea (Kandie, 2014). There was an attempt to amend the CBK Act and cap the lending rate at four per cent above the 91-day Treasury bill and the deposit rate at four per cent below the 91days Treasury bill. In 2013, the Kenya parliamentary budget office proposed the pegging of the deposit rate to the lending rate. The political leadership at the time pleaded with bankers to reduce the lending rate, and all that was widely ignored. For the past 20 years, Kenyan banks have been enjoying interest rate spreads of about 11.4 per cent on average way above the world average of 6.6 per cent (Kandie, 2014). However, in August 2016, the interest rate ceiling regulation was passed by parliament and signed by
the president, making it a legal requirement for banks and other financial institutions. The new amendments cap banks’ lending interest rates to no more than four per cent above the Central Bank Rate (CBR) currently at 10.5 per cent (Central Bank of Kenya, 2017). Therefore, the interest cap directly affected the financial performance of most commercial banks in Kenya (Kozak, 2016). When the law came into full force, interest rates dropped to a maximum of 14.5 per cent given the CBR’s current standing at 10.5 per cent (Central Bank of Kenya, 2017). Banks will also pay depositors 7.35 per cent on their money, forcing upon them the narrowest spreads since Kenya liberalized its financial markets in 1990s.

In Kenya, the Banking Sector is composed of the Central Bank, as the regulatory authority; Commercial Banks, non-Bank Financial Institutions and Forex Bureaus. By 2015, the banking sector comprised 44 institutions, 43 of which were commercial banks and 1 mortgage finance companies, 120 Foreign Exchange Bureaus. The six largest ones popularly known as Tier One control 52.4 per cent of the entire industry. This leads to only a few banks controlling the market, just like any other economy across the globe. The second–tier banks continue to wrestle out large banks in the control of market shares, with the share of deposits increasing particularly for medium banks and declining for large banks. Overall, there has been massive strategic shifts in the banking industry with: niche banks offering more options to consumers, increase in the number of banks to 42, 75% of the Kenyan population being served by various aspects of the financial sector, over 77% of Kenyans within 5kms of a service point, an increase of Agency Banking with over 35000 agents countrywide and an explosive growth of mobile money (Central Bank of Kenya, 2017). The Kenyan economy is free market with the central bank acting as a regulatory body.

Over the last few years, the banking sector in Kenya has continued to grow in assets deposits, profitability and products offering, leveraging on diversification to alternative channels, supported by favorable macroeconomic environment. The growth has been mainly underpinned by an industry with branch network expansion strategy both in Kenya and in the East African Community (EAC) region, automation of a large number of services and a move towards emphasis on the complex customer needs rather than traditional ‘off-the-shelf’ banking products. Players in this sector have experienced
increased competition over the last few years resulting to increased innovations among the players and new entrants into the market (CBK, 2015).

1.2 Statement of the Problem

Mbua (2017) conducted a study to ascertain the effects of interest rate capping by the CBK on banks listed in the Nairobi Stock Exchange. The study revealed that such interest rate regulation had a negative implication the banks’ share prices, with the Share prices dropping significantly after the interest rate cap law was enacted. Another study by Irungu (2017) revealed that interest rate capping reduces the spread earned by banks; negatively impacting the financial performance of financial institutions. The stocks that include Diamond Trust Bank, Kenya Commercial Bank (KCB) and Cooperative Bank, which all fall in the indicative 20 share index, were on a free fall as fears over the interest law spread at the bourse (Aligonby, 2016). The All Share Index similarly dropped by 5% to from 146.48 to 139.14 while the NSE 25 Share Index fell by 3 points to close the day at 3,913.93. The bond market saw 4.4 million worth of trades down from 18million (Maloba, 2016).

A consumer survey dated 22nd March 2017 commissioned by Kenya Bankers Association (KBA) and conducted by Nielsen states that 88% of the borrowers in the sample population did not change their borrowing behavior as a result of the rate cap. However, the same research also states that 77% of the sample would prefer a lower cost of credit than a higher deposit rate. The Monetary Policy Committee (MPC) Market Perception Survey conducted in March 2017 showed that private sector respondents expect a decline of growth in 2017, on account of the prevailing drought conditions and slowdown in private sector credit growth resulting from the 2016 interest rate cap. Following this legislation, the Markit Stanbic Bank Kenya Purchasing Managers’ Index (PMI) dropped to 49.9 in May 2017 from 50.3 the previous month, falling below the 50.0 level, which separates growth and contraction. The contraction is attributed to challenges in private sector access to credit, weak consumer demand due the CBK interest rate regulation.

When President Uhuru Kenyatta assented the bill into law of capping interest rates at 4% basis points above the CBR rate which currently stands at 9.5%, most stakeholders focused on the effects this would have on the end consumer of bank products (Mbua, 2017). Placing a cap on interest rates will impact the industry’s efficiency as it does not
account for several factors that might affect the bank’s decision to choose certain spreads. Therefore, the interest cap directly affected the financial performance of most commercial banks in Kenya. However, little attention was paid on how this new law could affect competition among banks. In addition, little has been done to reveal the strategies used by banks to create a competitive advantage. The objective of this study was to determine the effect of the interest capping regulation on commercial banks in Kenya.

1.3 General Objective
The general objective of this study was to assess interest rate capping on commercial banks in Kenya.

1.4 Specific Objectives
1.4.1 To determine the effect of interest rate capping on the competitiveness of banks in Kenya.
1.4.2 To assess the challenges posed to commercial banks by interest rate capping regulation.
1.4.3 To determine the strategies employed by commercial banks during interest rate capping.

1.5 Significance of the Study
1.5.1 Commercial Banks
By knowing how the market reacted to the capping of interest rates, banks may be able to find ways of ensuring they meet their overall objective of hedging competition. Banks may further find the results of this study useful in that they may use the findings to advise their customers on whether they should put their wealth in bank shares or find alternative industries to invest in. Moreover, banks may use the results of this study in making other inferences based on economic changes caused by interest rate caps.

1.5.2 Policy Makers
This study may be of importance to several groups of stakeholders since at the end of the day, the goal of any company is to maximize profits through market domination. The study may help the law makers to make policies with full understanding of the impact of the interest rate capping. If policies made are effective, there will be healthier economic growth, and this may be reflected in an active economy. The study also helps in
understanding the impact of interest rate spread on financial performance of the commercial banks in Kenya, aiding policy makers to carefully plan and forecast the impact of the policies with a view to ensure banks thrive to serve their purpose and at the same time to ensure customers are no exploited.

1.5.3 Regulators
The Central Bank of Kenya is mandated to regulate the operations of commercial banks and other financial institutions. This study provides further information to the Central Bank regarding the effeteness of the interest rate cap and its impact on the bank’s operation. With such information, the Central Bank, as a regulator, can revise or uphold the new law depending on the analysis they make. Another key regulator is the competition authority. This body regulates the operational strategies used by financial institutions to gain competitive advantage. This study provides information to help such authority establish if the banks are compliant with competition policies.

1.5.4 Bank Consumers
The various responses employed by banks when addressing the effects of interest rate caps are often consumer centered. Consumers may therefore ascertain the banks with the best customer service strategies. Consumers may also understand how the interest rate caps affect banking services. Moreover, customers may want to know which banks have the best rates, given the interest rate caps.

1.5.5 Researchers
Researchers may also benefit from the findings of this study as it reveals the various effects of interest rate capping and their impact on the banking industry. Since there are similar studies, this research provides existing research gap in relation to this topic. Thus, it is hoped that study stimulate further study on interest rate capping. Moreover, the findings of this study can be compared with strategic management in other sectors to draw conclusions on various ways an institution can respond to competitive forces in the environment.

1.6 Scope of the Study
The study was conducted within the Kenyan banking system. The study conducted, included the 43 commercial banks in Kenya. A sample of the banks were selected from
the list of banks provided by the Central Bank of Kenya. The study involved monitoring of the bank’s performance for the past year since the inception of the interest rate cap, that is, from September 2016 to August 2017.

1.7 Definition of Terms

1.7.1 Competitive Advantage
It is an advantage gained over the competitor offering customer greater value either through lower prices or by providing additional benefits and services that justify similar or possibly higher prices (Cole 2008).

1.7.2 Interest Rate Capping
This refers to a ceiling placed on interest rates, such that interest rates are allowed to fluctuate, but cannot surpass a stated interest cap (Maimbo et al., 2014). It dictates the maximum rate that a bank can charge its customers on loans, and in Kenya it is currently pegged on the CBR at 4%.

1.7.3 Competitive Advantage Strategies
This defines the ways a firm chooses to increase its competitive advantage. As elaborated by Porter (1980), a firm's competitive position within its industry determines whether a firm's profitability is above or below the industry average. The fundamental basis of above average profitability in the long run is Sustainable competitive strategies.

1.7.4 Commercial Banks
A commercial bank is a type of financial institution that accepts deposits, offers checking account services, and makes business, personal and mortgage loans, and offers basic financial products like certificates of deposit (CDs) and savings accounts to individuals and small businesses (Kaiba, 2016).

1.8 Chapter Summary
This chapter has presented the background information to the research problem, identifying the problem statement, the general objective of the study and the specific objectives that were addressed by the study. The chapter also presents the rationale, scope and definition of terms used.
Chapter two discusses the literature review, examining what other studies have done and what needs to be done while chapter three discusses the research methodology. Chapter four on the other hand brings in the research report which presents the results and findings while the last chapter, Chapter Five presents the discussion, conclusion and the recommendations of the study.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter covers a review of the relevant literature addressing the objective of this research. It covers the key concepts, purpose, theoretical and empirical framework. The literature review section discussed the existing theoretical and empirical studies relating to the research objective. Thereafter, an analysis was done to sum up the findings in this section, revealing the research gap and rationale of this study.

2.2 Effect of Interest Rate Capping on Commercial Banks

The modern theory of the banking firm seeks to establish the role of market structure and competition within the structural relationships faced by commercial banks, treating them as rational agents in an environment of risk and uncertainty. The theory of the banking firm studies the process of determining the price charged for the services offered by financial institutions (Kozak, 2016). On the role of structure and competition in the model, it is observed that three types of variables must be considered in the analysis of the fees that the banks offer to deposits. These are: the economic variables, the market structure and the degree of interbank competition. The banking spread reflects the degree of monopoly of the bank, therefore, is an increasing function of the degree of concentration of the banking sector as a whole (Silva et al., 2007). Therefore, banks will demand a positive interest spread or fee as the price of providing depository and loan service in face of the uncertainty generated by operating environment (Kozak, 2016).

Before interest rates were capped the interest rate on loans, deposit and mortgages were being determined by the banks individually. The interest rates were very high and the banks were performing very well. According to the supervisory report of the central bank annual report (2015) the banking sector has remained stable and resilient 2015 as evident by 9.2% of growth in the banking sectors balance sheet from Ksh 3.2 trillion in December 2014 to Ksh 3.5 trillion in December 2015. This is despite the slowdown in global economic growth to 3.1 per cent in 2015 from 3.4 per cent in 2014 largely due to slowdown in growth in China and the sluggish recovery in the Euro zone. Currently the interest rates are restricted (Muthuva, Muriuki & Egondi, 2017).
2.2.1 Reduction in Market Power

Competition in the banking sector has been analyzed by measuring market power, that is, a reduction in competitive pressure and efficiency. A well-known approach to measuring market power is suggested by Bikker (2003). The author analyzes bank behavior on an aggregate level and estimate the average conjectural variation of banks. A strong hypothetical variation implies that a bank is highly aware of its interdependence, through the demand function, with other banks in terms of output and prices (Kozak, 2016).

Under perfect competition, where output price equals marginal costs, the hypothetical variation between banks should be zero, whereas a value of one denotes a monopoly (Osei-Assibey & Bockarie, 2013). Another indicator for market power is the Herfindahl-Hirschman Index, which measures the level of market concentration. This indicator is often used in the context of the ‘Structure Conduct Performance’ (SCP) model, which assumes that market structure affects commercial banks’ behavior, which in turn controls their performance (Faizan, 2016). The idea is that banks with larger market shares may have more market power and use that. In addition, a smaller number of banks make collusion more likely. Market power may also be related to profits, in the sense that extremely high profits may be indicative of a lack of competition (Bikker, 2003).

2.2.2 Decrease in Financial Performance

Interest rate defines the rate of interest charged for the amount of money borrowed. Financial institutions usually have general guidelines for the rate they intend to charge. Money borrowed by the bank on short-term or long-term basis has different interest rate. The interest rate parity condition was developed by Keynes (1933) to link the exchange Rate, interest rate and inflation. The theory also has two forms: covered interest rate parity (CIRP) and uncovered interest rate parity (UCIRP). CIRP describes the relationship of the spot market and forward market exchange rates with interest rates on bonds in two economies (Ngugi, 2001). UCIRP describes the relationship of the spot and expected exchange rate with nominal interest rates on bonds in two economies. This is the normal form of the covered interest rate parity, which states that the domestic interest rate must be higher than the foreign interest rate by an amount equal to the forward premium (discount) on domestic currency (Ngugi, 2001).
Interest rates, inflation, and exchange rates are all highly correlated (CBK, 2012). By manipulating interest rates, central banks exert influence over both inflation and exchange rates, and changing interest rates impact inflation and currency values. Higher interest rates offer lenders in an economy a higher return relative to other countries. Therefore, higher interest rates attract foreign capital and cause the exchange rate to rise. The impact of higher interest rates is mitigated, however, if inflation in the country is much higher than in others, or if additional factors serve to drive the currency down. The opposite relationship exists for decreasing interest rates- that is, lower interest rates tend to decrease exchange rates (Bergen, 2010).

The performance of commercial banks depends on a wide range of business, but interest rates still play a key role in determining the financial performance and the effective competitive strategies to be employed (Priti, 2016). Priti (2016) assessed the mean and volatility spill overs resulting from changes in short-term interest rates and exchange rates, and long-term interest rates and exchange rates. Interest rates have a direct effect on the activities of commercial banks because it is believed that they affect their financial performance (Priti, 2016). The valuation of bank assets is the most important factor when it comes to the valuation of bank stocks followed by the rise and fall of interest rates. Conventionally, retail banks make money by relying on the relationship between interest rates, deposits and the market competition. This implies that bank loan rates tend to be lower under heavier competition, thus improving social welfare. Banks compensate for stronger loan market competition by lowering their deposit rates. Furthermore, evidence is found for all four loan categories that, in the long run, bank Loan rates are closer in line with market rates where competition is higher (Gulati et al., 1998). These results show that stronger loan market competition reduces bank loan rates while changes in market rates are transmitted more rapidly to bank rates. These findings underline that bank competition may have a substantial impact on the monetary policy transmission mechanism (Priti, 2016).

In 2015, the People’s Bank of China took a major step by eliminating the ceiling on interest rates on deposits (Ngai, Qu & Yung, 2016). The move came two years after the central bank abandoned the floor for interest rates on loans, representing the final step in liberalizing interest rates in the country. Banks operating in China had to adjust to a much more competitive environment. The liberalization posed significant challenges for banks
accustomed to a highly regulated market. But it also presented valuable opportunities, especially for small and mid-sized banks that used their newly-found flexibility to implement smarter business strategies that propelled them to the head of the industry (Carr & Seto, 2013). Such strategies increased margins while drawing lending and deposit clients from their bigger rivals. According to Ngai, Qu, & Yung (2016), banks wishing to succeed in the transition, a crucial component of their transformation programs must be a sophisticated pricing system. Adopting modern pricing processes can deliver a significant boost in revenues, provide improved services for the dominant corporate banking segment, and support management performance improvements in the mid- and back offices (Zhang, Ralescu & Liu, 2016).

Ngai, Qu, & Yung (2016) further argue that a sophisticated pricing system will also have ripple effects on a bank’s middle- and back office management performance. Coming from a highly regulated regime, banks in China generally lacked capabilities for determining exact baseline costs for individual products, and as a result had trouble establishing crucial metrics such as funds transfer pricing, risk, economic capital, and cost allocation. The rigors of sophisticated pricing systems forced banks to correct these deficits, enhancing the professionalism of their middle- and back-offices. Improved performance in the middle- and back-offices translated directly into competitive advantages (Zhang, Ralescu & Liu, 2016). For example, above-average efficiency for a given product would allow the bank to offer more attractive prices or capture higher margins, either of which improves its market position. Clear metrics also provided other benefits. For instance, products determined to have excessively high input-output ratios, can be corrected with price adjustments and such data can support decisions on whether to invest further in a product, outsource all or part of operation, try to create economies of scale through mergers and acquisitions, or even drop the product altogether (Ngai, Qu & Yung, 2016).

Another study by Zhang, Ralescu and Liu (2016) on the interest rate ceiling in China before financial liberation indicates that the corporate banking sector accounts for more than 60 percent of total banking revenues in China. During the interest cap era, the bank management capabilities improved greatly in retail banking, while they languished in corporate banking. In corporate banking, client management was often left to unplanned decisions by relationship managers under the assumption that frontline staff had a better
understanding of what the market could bear (Ngai, Qu & Yung, 2016). Sophisticated pricing helped banks build better relationships with corporate clients. These modern pricing systems focus on client needs, rather than an overarching performance metric. Zhang, Ralescu and Liu (2016) further reveal that planning a strategy around each major corporate account requires collaboration among relationship managers, team leaders, product managers, and risk managers, among others. The result is a product package designed for individual corporate needs, a level of attention that can create closer relationships. In addition, sophisticated pricing systems not only suggest optimal prices, but also identify potential cross-selling opportunities.

2.3 Challenges of Interest Capping on Commercial Banks

From an economic perspective, input based solutions like interest rate caps or subsidies distort the market and hence it would better to let the market determine the interest rate, and to support certain desirable sectors through other means (such as output based aid (Acharya, Santos & Yorulmazer, 2009). Indeed there are a number of other methods available that can contribute to a reduction in interest rates. In the short term, soft pressure can be an effective tool – as banks and Monetary Financial Institutions (MFIs) need licenses to operate, they are often receptive to influence from the central bank or regulatory authority (Xinhua, 2017).

The paradigm of classical economics runs that competition between financial institutions should force them to compete on the price of loans that they provide and hence bring down interest rates. Competitive forces can certainly play a role in forces lenders to either improve efficiency in order to bring down overheads, or to cut profit margins (Brooke & Oliver, 2005). In a survey of MFI managers in Latin America and the Caribbean, competition was cited as the largest factor determining the interest rate that they charged. The macro evidence supports this view – Latin countries with the most competitive microfinance industries, such as Bolivia and Peru, generally have the lowest interest rates (Xinhua, 2017).

The corollary of this, and the orthodox view, would seem to be that governments should license more financial institutions to promote competition and drive down rates. However it is not certain that more players means greater competition (Djibril, 2013). Due to the nature of the financial sector, with high fixed costs and capital requirements, smaller
players might be forced to levy higher rates in order to remain profitable. Weak businesses that are inefficiently run will not necessarily add value to an industry and government support can often be misdirected to supporting bad businesses (Acharya, Santos & Yorulmazer, 2009). Governments should be willing to adapt and base policy on a thorough analysis of the market structure, with the promotion of competition, and the removal of unnecessary barriers to entry such as excessive red tape, as a goal (Hurn & Farl, 2007).

The evidence suggests that learning by doing is a key factor in building up efficiency and hence lowering overheads and hence interest rates. Institutions with a decent track record are better able to control costs and more efficient at evaluating loans while a larger loan book will generate economies of scale (Landerman, 2000). More established businesses should also be able to renegotiate and source cheaper funds, again bringing down costs. In China, the government supports the financial sector by setting a ceiling on deposits and a floor on lending rates meaning that banks are able to sustain a minimum level of margin (Acquaah & Yasai-Ardekani, 2008). Following an international sample of MFIs, there is clear evidence from the microfinance information exchange that operating expenses fell as a proportion of gross loan portfolio as businesses matured.

The implication of this is that governments would be better off addressing the cost structures of financial institutions to allow them to remain commercially sustainable in the longer term (Marciukaityte, Roskelley & Wang, 2009). For example, government investment in credit reference bureaus and collateral agencies decreases the costs of loan appraisal for banks and MFIs. Supporting product innovation, for example through the use of a financial sector challenge fund, can bring down the cost of outreach and government support for research and advocacy can lead to the development of demand-led products and services (Landerman, 2000). The FinMark Trust is an example of donor funds supporting the development of research and analysis as a tool for influencing policy.

2.3.1 Managing Interest Income
Interest financial gain is one of the most pronounced sources of revenues for commercial banks. Regulation of interest rates is therefore expected to bring an instantaneous impact on the interest income of these banks (Hurn & Farl, 2007). It is therefore paramount to
grasp the impact the regulation of capping of interest rate has on the banks which is mainly wearing margins on interest financial gain (Teern, 2011).

Profitability and monetary performance is measured by how well the management uses company’s assets to come up with profits (Rug, 2013). Interest rates have an effect on profits of banks directly (Aren & Duhn, 2016). In line with Hurn and Farl (2007), interest rates have an effect on bank gain either directly or indirectly. Low interest rate may mean additional population seeking credit financing and banks profit could be impacted by redoubled interest earnings in this scenario. Conversely, redoubled interest rates discourage shoppers from borrowing and this results in reduced interest financial gain generated and successively reduced profits of the bank (Teern, 2011).

When banks impose several necessities for purchasers to access loans, the demand decreases and this lowers the 2number of interest financial gain earned. Implementation of interest capping encourages additional informal borrowing as customers elect the additional simply accessible loans that ultimately have a bearing on formal banking sector credit demand and ultimately bank gain (Rosenberg, Gonzalez & Narain, 2009). Ngugi aforementioned that the economic and business Development Corporation (ICDC) declared a three-percentage purpose reduction in loan interest because it fought to retain a competitive edge underneath the new rate capping era that forced banks cut charges in this African country (Industrial and business Development Corporation (ICDC, 2016).

2.3.2 Credit Risk and Default Risk Management

Because of interest rate capping, banks have less appetite to supply unsecured to individuals or organizations including Small and Medium Enterprises (SMEs) perceived to be more risky (Rosenberg, Gonzalez & Narain, 2009). Interest rate capping slows down the flow of credit to some specific sectors perceived to be riskier and leads to increased transaction fees and commissions charged to compensate for the expected decreased in earnings (Osei-Assibey & Bockarie, 2013). For the banks to manage credit risk, they need to extend the chance premium that successively will increase the disposal rate (Apanga, Appiah & Arthur, 2016). With the emergence of interest rate capping, banks are unable to maintain an economic interest rate spread and thus they are exposed to credit risk and at last this leads to reduction of profits (Edris, 1997). As survival technique banks increase other facility fees for borrowing like processing fees,
negotiation fees, insurance fees which ultimately makes the loans more expensive and discourages individuals from borrowing and saving (Rosenberg, Gonzalez & Narain, 2009).

Implementation of interest rate capping forces banks to have high restrictive and thorough background checks on customers before advancing credit to them. In other words these financial institutions adopt low risk appetite disposition. This type of approach discourages customers from approaching the formal banking sector for credit. Faizan (2016) dispensed a study to analyze the impact of economic reforms, monetary easing and banking regulation and policies focusing on seventy-six economies and concluded that monetary reform and specifically interest rate capping had a negative and statistically vital impact on bank interest margins.

A research in German and Great Britain banks revealed that the changes on the capping law and banking rules reshaped almost each German and Great Britain banking establishments (Stevenson, 2016). The German bank staffs were facing an ever-increasing pressure as their employers attempt to become economical, streamlining banks with a high orientation towards their shareholders during an extremely competitive market. Borrowers may hide information regarding their personal assets and expose the banks to default risk and great difficulty for the financier to call up the debt. When in an ongoing contract conditions the terms between the loaner and the borrower changes, a financial loss may occur (Ekpu & Paloni, 2016). This normally happens when a recipient does not come up with provision for future payments because of unwillingness to pay his or her debts, or just in case of terminated employment. This definitely increases volatility and default risk. Failure to honor payments to the bank ultimately leads to diminished profits, because the interest financial gain isn’t earned at the side of the principal quantity. Increase in default risk, forces banks to extend interest rates and so decreases volatility (Agrawal & Maheshwari, 2014).

At the Back drop of interest rate capping, the banks are unable to extend the interest rate and this implies volatility is high and consequently high default risk. There exists a direct relationship between default risk and volatility. A research study done in Turkey found that there exists an important relationship between volatility and a default state of the loaning contracts, (Osken, Onay & Unal, 2016).
2.3.4 Forced Cost Cutting Measures

Competition at the backdrop of interest rate capping forces banks to shut down thanks of some of the branch to reduce operational costs. Banks are pressured to offer loans at low interest fees which might be unable to cover the loan expenses (Osei-Assibey & Bockarie, 2013). In effort to cover gap caused by interest rate capping, banks for instance upload mortgage charges (like commissions) in an effort to keep away from default of loans (Edris, 1997). These extra prices make borrowers to seek credit in the informal market resulting to reduced profits or losses for the mainstream banking. In the year 2017 Kenyan Banks let go of 1,620 staff as they took proactive measures aimed at increasing operational efficiency in response to a challenging operating environment, with the interest rate capping being one of the main contributors (Cytonn Research Team, 2018).

2.4 Strategies Used by Commercial Banks during Interest Rate Capping

Commercial banks respond to interest rate capping with strategies to gain competitive advantage so as to survive and remain profitable. Competitive advantages are the conditions that allow the productive entity to generate more sales or superior margins than its competition. Competitive advantages are attributed to a variety of factors, including cost structure, brand and quality of product offerings, distribution network, intellectual property and customer support (Porter, 2014). On the other hand, competitive advantage strategies define the ways a firm chooses to increase its competitive advantage. As elaborated by Porter (2014), a firm's competitive position within its industry determines whether a firm's profitability is above or below the industry average. The fundamental basis of above average profitability in the long run is sustainable competitive strategies.

The importance of competitive strategies on performance of an organization is examined by different authors. According to Porter (2014), organizations with defined strategy outdo the ones without a strategy. This proposition is the foundation for the strategies for creating a competitive advantage. Porter (2000) further argued that higher performance can be achieved in a competitive industry through the pursuit of a generic strategy which include development of an overall cost leadership, differentiation, or focus approach to industry competition. Porter argued that a company without any of strategies it will exhibit lower performance as compared to the firms following a strategy. Moreover, a firm trying to mix two strategies will be caught up in between and will also achieve lower
performance. Low cost and differentiation strategies are founded on dissenting assumptions and thereby generate trade-offs within the organization.

2.4.1 Cost Differentiation Strategy
A firm implementing a differentiation strategy is able to achieve a competitive advantage over its rivals because of its ability to create entry barriers to potential entrants by building customer and brand loyalty through quality offerings, advertising and marketing techniques. Thus, a firm that implements a differentiation strategy enjoys the benefit of price inelastic demand for its product or service (Hyatt, 2001). The successful implementation of the differentiation strategy requires resources and skills. Firms that implement a cost leadership strategy are able to secure a relatively large market share by being the lowest cost producers or service providers in their industry or market (Cole, 2008). Thus, firms implementing the cost leadership strategy can obtain above-normal profits because of their ability to lower prices to match or even below those of competitors and still earn profits (Ramsey, 2013).

Lower costs and cost advantages result from learning curve benefits, economies of scale, process innovations, product designs, reengineering activities and reducing manufacturing time and costs (Bauer & Colgan, 2001). Only one organization in an industry can be the cost leader and if it’s the only difference between the organization and competitors, the best strategic choice is the low-cost leadership role (Malburg, 2000). An organization could become a low-cost leader by enjoying access to the raw material in terms of proximity and having technology which assist in lowering of costs (Bauer & Colgan, 2001). Because of lower cost, the demand rises, increasing the sales and eventually the firms share in the market (Helms et al., 2007). If a firm is a leader in terms of low-cost, this gives that firm competitiveness which act as entry barrier for rivals who would need intensive capital to penetrate the market (Hyatt, 2001).

The reason for applying the strategy of cost leadership is to obtain the advantage by reducing the economic costs among its competitors (Barney, 2002). This strategy highlights operational efficiency. By producing high qualified and standardize products or services, at the same time, with the effects of the economic scale and experience curve, the firm strives to gain a sustainable competitive advantage among its competitors (Helms et al., 2007). Basically, the firm has two major ways to main this cost advantage. Either
by controlling the cost drivers, which means that a firm can gain an advantage according to the cost drivers of value activities disclosing a profound proportion of total cost; or by reconfigure the value chain, in other words, with the adoption of different and more efficiency way to manufacture, promote, distribute and design the product, a firm can also gain a cost advantage (Porter, 2014).

2.4.2 Product Differentiation Strategy
Product differentiation strategy can be a tool of competitive advantage which is adopted by organizations to provide products that satisfies individual customer’s needs. In satisfying individual customer’s needs, quality has become a major differentiating factor among products (Shammot, 2011). As a result, customers are willing to pay more for products that cater to their individual size, taste, style, need or expression. Hence, achieving competitive advantage through product differentiation becomes the focus of this study. The study findings of Acquaah and Yasai-Ardekani (2008) show the viability and profitability of implementing cost leadership, differentiation, and the combination of the singular strategies. Nevertheless, the incremental performance benefits to firms implementing a combination strategy do not significantly differ from the performance of firms implementing only the differentiation strategy. In addition, firms that implement a coherent competitive strategy (combination, cost-leadership, or differentiation) tend to gain considerable incremental performance benefits.

2.4.3 Diversification Strategy
Diversification helps a bank in eliminating the unevenness of geographical reach, product-process innovation, exploit economies of scale and scope, reap benefit of advanced technology, and diversify risk along with mobilization of additional capital. Diversification has opened the door for commercial banks to earn fee income from investment banking, merchant banking, insurance agency, securities brokerage, and other nontraditional financial services. Acharya et al. (2002) classify the banks’ motive to diversify as synergy (or economic) motive, managerial motive, value maximization motive, increased market power motive, capital strength and risk diversification motives. Determinants of diversification can be categorized into two categories; External determinants such as economies of scale and scope, dynamics of bank competition, global presence of financial conglomerates and disintermediation in banking activities. The
internal determinants include risk reduction motive, decline in interest margin, cost of production, low cost of capital, and technology upgradation (Acharya et al., 2002).

Basically, the variety of diversification strategies in the banking sector can be summarized under four main headings. The first is Direct Cross-Border Sales which means trade of financial services without any physical presence of banks in target markets (Tabak et al., 2011). A low contribution to the integration of retail marketing is achieved by direct cross-border sales of financial services. This category comprises telephone banking, conventional mail marketing and, in particular, internet banking. The second strategy is the establishment of branches or subsidiaries in the target country (Acquaah & Yasai-Ardekani, 2008).

Mergers and Acquisitions (M&A) constitute the third strategy (ECB, 1999). These are usually followed by considerable modifications in the organizational and legal structure of the respective Companies. In addition to mergers and acquisitions within the banking sector, a number of cross-industry mergers and acquisitions involving banks can also be observed. In particular, large banks diversify their business fields with the objective of reaching broad market coverage in financial services (one-stop finance) (Willman, 2000). Not only capital investment companies (for example, fund companies), but also insurance companies are the target objects of mergers and acquisitions in the banking sector. Finally, diversification strategy can be achieved by Cooperation and Strategic Alliances. Here, it is decisive that there is only a minority stake. Literature on diversification in the banking industry suggests that there exists several type of diversification: geographical, source of income, product/services, and economic sectors (Tabak et al., 2011).

The concept of strategic alliance has been defined by many scholars in their studies. Brooke and Oliver (2005) suggest that the alliance is an agreement between parties formed to advance common interests or causes in an attempt to achieve a particular aim. Organizational nature, Gulati et al. (1998) define strategic alliance as a voluntary arrangement between firms involving exchange, sharing, or co-development of products, technologies, or services. In order to take advantage of potential growing opportunities, modern corporations undertake various actions, including growing internally, issuing licenses, forming strategic alliances, setting up new joint ventures, or acquiring minority interest from other firms. Compared with M&A or formations of joint venture, strategic
alliance is a relatively flexible and easy operated approach for inter-firm collaboration to seize the growth opportunity (Marciukaiyte et al., 2009). Therefore, forging strategic alliances have been employed by more and more corporations in recent years.

Landerman (2000) explores potential diversification benefits to be had from banks merging with non-banking financial service firms. Simulated mergers between US banks and non-bank financial service firms show that diversification of banks into insurance business and securities brokerage are optimal for reducing the probability of bankruptcy for bank holding companies. Wheelock and Wilson (2004) find that expected merger activity in United States (US) banking is positively related to management rating, bank size, competitive position and geographical location of banks and negatively related to market concentration.

2.5 Chapter Summary
This chapter provides the literature review and it lists the specific strategies used by the financial institutions and how they are measured. The review further discusses the meaning of interest rate capping and how it affects commercial banks. This section brought into perspective the various empirical studies relating to interest rate capping and competitive advantage strategies. As evident, no study has been done in, especially in Kenya, to show how commercial banks adjust their competitive advantage strategies in response to interest rate caps. Moreover, none of the studies has documented the competitive advantage strategies used by banks after the interest rate cap. Chapter three follows with an elaboration of the research techniques that were applied.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

The chapter presents a logical sequence on how the study was carried out in order to answer the research objectives highlighted in chapter one of this study. It presents the design, identifies the population of study and presents the data collection method, research procedures and data analysis method.

3.2 Research Design

Berman-Brown and Saunders (2008) define research design as a guide for conducting a study with maximum control over factors that may interfere with the validity of the findings. A research design is a plan that defines how, where and when the data was be collected and analyzed (Saunders & Rojon, 2014). The study adopted a cross-sectional survey design. The descriptive study method was appropriate because it explores and describes the relationship between variables in their natural setting without manipulating them. The descriptive study aims at obtaining information that can be analyzed, patterns extracted, and comparison made for the purpose of clarification and provision of basis for making decisions. This design method was selected on the basis that it can collect diverse information types and is quick and less costly.

Jorde (2008) states that cross sectional survey is aimed at determining the frequency of a specific attribute, in a defined population at a given point in time. Quantitative data was obtained for comparison purposes. The study used the cross sectional survey design because it sought to answer the question of what is going on which is an important aspect to consider for social researchers. The design was used in this study to examine the effect of interest rate capping on commercial banks in Kenya.

3.3 Population and Sampling Design

3.3.1 Population

A research population refers to a well-defined collection of individuals or objects known to have similar characteristics (Saunders, Lewis & Thornhill, 2012). Creswell (2008) also define population as the total body of individuals or objects in a scientific query. The population of interest this research study comprised of top and middle marketing managers from tier 1 Commercial Banks within Nairobi County. There were 6 banks
within the Nairobi County with a total of 240 commercial bank marketing managers which made up the population target and were distributed as shown on Table 3.1.

Table 3.1: Population Distribution

<table>
<thead>
<tr>
<th>Commercial Bank</th>
<th>Number</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Barclays Bank of Kenya Ltd</td>
<td>40</td>
<td>17</td>
</tr>
<tr>
<td>Standard Chartered Bank</td>
<td>10</td>
<td>4</td>
</tr>
<tr>
<td>Co-operative Bank of Kenya Limited</td>
<td>50</td>
<td>21</td>
</tr>
<tr>
<td>Kenya Commercial Bank Limited</td>
<td>55</td>
<td>23</td>
</tr>
<tr>
<td>National Bank Limited</td>
<td>15</td>
<td>6</td>
</tr>
<tr>
<td>Equity Bank</td>
<td>70</td>
<td>29</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>240</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Central Bank of Kenya (2018)

3.3.2 Sampling Design

3.3.2.1 Sampling Frame

According to Rojon and Saunders (2012) a sampling frame is the set of source materials from which sample is selected. Hair, Black, Babin and Anderson (2013) state that, a sampling frame is the source material or device from which a sample is drawn. It is a list of all those within a population who can be sampled, and may include individuals, households or institutions. In this study, the sampling frame consisted of the list of branch managers of the 6 banks in Kenya located in Nairobi County and 240 marketing managers which was obtained from the Central Bank report.

3.3.2.2 Sampling Techniques

The sampling embraced a mixed method approach to sampling techniques involving stratified sampling technique and simple random sampling (SRS). Stratified sampling technique is a probability sampling technique wherein the researcher divides the entire population into different subgroups or strata, then randomly selects the final subjects proportionally from the different strata (Berman-Brown & Saunders, 2008). For this study, the researcher divided the population into 6 study strata for top managers and middle managers from the 6 commercial banks that were the study target (Barclays Bank

Simple random sampling was then applied to select individual respondents from each study strata. Hair et al. (2013) observes that SRS is a sampling technique where every item in the population has an even chance and likelihood of being selected in the sample. Here the selection of items completely depends on chance or by probability and therefore this sampling technique is also sometimes known as a method of chances. This method was preferred in the study because it did not introduce any biasness during the sample size determination and section.

3.3.2.3 Sample Size

Sample size determination is the act of choosing the number of observations or replicates to include in a statistical sample. The sample size is an important feature of any empirical study in which the goal is to make inferences about a population from a sample (Creswell, 2008). According to Saunders (2012), note that, though a relatively straightforward concept, choice of sample size is a critical determination for a project. Too small a sample yields unreliable results, while an overly large sample demands a good deal of time and resources. For this study, the sample size was determined using the Yamane formula as shown:

\[ n = z^2 \times p(1-p) + e^2 \]

Where:

- \( n \) = required sample size
- \( z \) = Confidence Level at 95% (standard value of 1.96)
- \( p \) = population reliability; where \( p \) is 0.5 which is taken for population
- \( e \) = Margin of error at 5% (standard value of 0.05)

\[ n = 1.96^2 \times 0.5(0.5) = 0.12 \]
\[ = 96.04 = 96.04 \times 240 = 96.04 + 240 \]
\[ = 68.59 \]
\[ = 68 \text{ Marketing Managers who were distributed as shown on Table 3.2} \]
Table 3.2: Sample Size Distribution

<table>
<thead>
<tr>
<th>Commercial Bank</th>
<th>Number</th>
<th>Percentage</th>
<th>Sample Size</th>
</tr>
</thead>
<tbody>
<tr>
<td>Barclays Bank of Kenya</td>
<td>40</td>
<td>28.5</td>
<td>11</td>
</tr>
<tr>
<td>Standard Chartered Bank</td>
<td>10</td>
<td>28.5</td>
<td>3</td>
</tr>
<tr>
<td>Co-operative Bank of Kenya</td>
<td>50</td>
<td>28.5</td>
<td>14</td>
</tr>
<tr>
<td>Kenya Commercial Bank</td>
<td>55</td>
<td>28.5</td>
<td>16</td>
</tr>
<tr>
<td>National Bank Limited</td>
<td>15</td>
<td>28.5</td>
<td>4</td>
</tr>
<tr>
<td>Equity Bank</td>
<td>70</td>
<td>28.5</td>
<td>20</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>240</strong></td>
<td><strong>28.5</strong></td>
<td><strong>68</strong></td>
</tr>
</tbody>
</table>

3.4 Data Collection Method

This study applied questionnaires collected from respondents as primary data. The objective of this study was to assess the effect of interest rate capping among the Kenyan commercial banks and the key instrument that was used was self-administered questionnaires.

Self-administered questionnaire is a data collection technique in which the respondent reads the survey questions and records his or her own responses without the presence of a trained interviewer (Rojon & Saunders, 2012). Whereas self-administered questionnaires present a challenge of heavily relying on the clarity of the written word more than on the skill of interviewer, this method has a number of advantages, for instance, the questionnaire can be completed whenever respondents have time (Berman-Brown & Saunders, 2008). In this study, the respondents who wished to take the questionnaire to fill in their responses at their convenience at return to their branches/offices were allowed to do so.

A standardized questionnaire that captures the various variables under study was adopted. A questionnaire is an instrument that gathers data over a large sample and its key objective is to translate the chosen objectives into specific questions so as to elicit the answers for each of the question (Carr & Seto, 2013). The use of a questionnaire with standardized data enables a researcher to collect large amount of data from a sizeable population in a highly economical way and it also allows easy comparison (Saunders et al., 2012).
The questionnaire had four sections. The general section (section A) of the questionnaire was to get the general profile of the respondents and the enterprises including their identity but whose response was optional. Section B focused on effects of the interest rate cap to commercial banks, Section C focused on the challenges faced by commercial banks, while Section D focused on the strategies adopted by commercial banks during the rate cap. The questionnaire also employed a 5 point Likert scale that measured the different aspects of the study variables. The responses that were outlined on the Likert scale ranged from: 1. strongly disagree, 2. Disagree, 3 Neutral 4. Agree 5. Strongly agree.

3.5 Research Procedures
The first step was to conduct a pilot survey to ascertain the response rate and any other problem likely to be experienced during data collection. The pilot survey was done by the researcher, with the help of a few research assistants. In the pretest, the questionnaires were administering to between 10 and 15 top and Middle marketing managers from the selected banks. The pretest gauged the ability of the research assistants to execute the research plan without difficulties.

The data collection employed a drop and pick strategy for administering the questionnaires. A research assistant after giving a brief on the objective of the study and assuring the respondents of confidentiality allowed the respondent’s time to fill the questionnaire before collecting. The questionnaire consists of four sections using a summated rating method, which required respondents to tick the number that most accurately reflected their opinion on each statement. The design of the questionnaire was based on multiple-item measurement scale.

In another strategy, research assistants were recruited to administer the questionnaires to the identified respondents who wished to fill in their responses, and also to provide any support required by the respondents. The research assistants were trained on knowledge and skills on basic interview skills and filling in responses in the questionnaires, selection and sampling of study participants as well as their roles and responsibilities during the data collection period. The criterion for selection of the research assistants included possession of at least a diploma level certificate of education and fluency in English and Swahili. The research assistants were subjected to pre-testing of the questionnaire in order
to identify some of the challenges expected and also to assess the level of success of the training. Successful trainees were considered for data collection exercise with supervision to ensure data quality assurance and consistency.

During the data collection period, after the researcher secured permission from the branch managers to allow for data collection, the research assistants administered the questionnaires to the identified managers. For the respondents who opted to complete the questionnaire immediately, they were allowed maximum time to complete and give the completed questionnaires to the research assistants. However, participants who wished to carry the questionnaire to complete at their convenience, the questionnaires were put in an envelope, given to the participants and requested to fill in and return to the branch/office from which the concerned research assistants collected the returned questionnaires after a period of one week. To ensure a high response rate, the research questionnaire was simplified.

3.6 Data Analysis Methods
Field (2013) states that decisions about data entails activities which encompass the following processes: scrutinize, edit, convert and modeling data to extract meaningful information, suggestions and conclusions that guide towards making relevant decisions. Quantitative data was collected and analyzed using descriptive statistics, inferential statistics (correlations and multiple regressions). Descriptive statistics such as mean, standard deviation and frequency distribution was conducted to analyze the data. The descriptive analysis gave useful summaries while the inferential analysis was helpful in identify variable relationships. Data presentation was done by use of tables and figures. The regression equation for the study was in the form of \( Y = a + B1X1 + B2X2 + B3X3 \).

3.7 Chapter Summary
This chapter has presented a logical sequence on how the study was carried out in order to answer the research objectives highlighted in chapter one of this study. It has shown the appropriate research design, identified the population of study and the data collection tools, the research procedures and data analysis method. Most importantly, it has outlined the sampling techniques that were used along with the data analysis methods. The next chapter documents the results and findings of the study.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction
This chapter presents the findings of the study. The main objective of the study was to assess the effects of interest rate capping on Kenya banks. The prevailing interest rate data used was obtained from various banks. The study used descriptive and inferential analytical techniques to analyze the data obtained. The findings were presented using tables, and graphs for simplified discourse. The first part of the analysis considers the demographics of the population used in the study. The chapter concluded with a chapter summary.

4.2 Response Rate and Demographic Information

4.2.1 Response Rate
Out of total of 68 questionnaires issued, 68 responses were received from various banks which represented 100% response rate achievement. The high response rate was attributed to the good relationship created with the senior management team, and the follow-up method that was employed by the researcher and the team.

4.2.2 Gender of Respondents
Figure 4.1 shows that 57.4% of the respondents were female and 42.6% were male. This means that majority of the top and middle managers in the Kenyan banking industry were female which could be explained by the national population of the country that has more females than males.

Figure 4.1: Gender of respondents
4.2.3 Age of Respondents
The study sought to establish the ages of the respondents and the findings revealed that those aged below 30 years represented 26.5%, while those aged between 31-40 years representing 62.8%, while those aged between 41-50 years representing 10.3%, 51-60 years was represented by 1.5%, and none was above the age of 61 years as indicated in Figure 4.2. This implies that the firms have a majority of relatively young employees who are able to steer the company into the future. There was no respondent above 60 years of age.

Figure 4.2: Age of Respondents

4.2.4 Job Level of Respondents
The study sought to establish the job level of the respondents and the findings revealed that 94.1% were middle level managers and 5.9% were top level managers as indicated in Figure 4.3. This implies that all targeted firm managers were captured in the study making it conclusive for both spectrum of managers.

Figure 4.3: Job Level of Respondents
4.2.5 Years in the Organization
The study sought to establish the number of years the managers had been with their respective organizations and the findings revealed that those who had worked for 21 years and above represented 60.3%, those who worked for 6-10 years represented 19.1%, while those that worked for 11-15 years represented 10.3%, those who worked for 16-20 years represented 2.9%, and none had worked for less than a year. This implies that the managers had worked for more than 5 years making them proper candidates for the study.

![Figure 4.4: Years in the Organization](image)

4.2.6 Size of Bank based on Capital Base
The study sought to establish the size of bank based on the capital base and the findings revealed that 48.5% of the banks had a capital base of 16 billion and above, 29.4% had a capital base of 1-5 billion, 11.8% had a capital base of 6-10 billion, and 10.3% 29.4% had a capital base of 11-15 billion. This indicates that majority of the tier 1 banks had a good capital base.

![Figure 4.5: Size of Bank based on Capital Base](image)
4.2.7 Number of Employees
Figure 4.6 presents the findings that reveal that respondents working for banks with more than 5000 employees were the majority, 25%, while respondents from banks with employees below 500 and between 500-1000 were almost equal at 22.1% and 22.2% respectively. Respondents from the banks with employees between 1000-3000 and 3000-5000 contributed the least with 17.6% and 13.2% respectively.

Figure 4.6: Number of Employees

4.3 Effect of Interest Rate Capping on Commercial Banks
4.3.1 Rating of the Effect of Interest Rate Capping on Banks
Table 4.1 shows that interest rate capping has reduced bank profits as indicated by 82.4% of the respondents who agreed while 13.2% disagreed and 4.4% were neutral with a mean of 4.26 and a standard deviation of 1.128. Interest rate capping has increased risk and operation cost as indicated by 51.4% of the respondents who agreed while 29.4% disagreed and 19.1% were neutral with a mean of 3.41 and a standard deviation of 1.458. Interest rate capping has increased access to finance to small corporations as indicated by 48.6% of the respondents who agreed while a significant percentage of 45.5% disagreed and 5.9% were neutral with a mean of 3.07 and a standard deviation of 1.669. Interest rate capping has reduced supply of credit as indicated by 82.4% of the respondents who agreed while 13.2% disagreed and 4.4% were neutral with a mean of 4.12 and a standard deviation of 1.127.
### Table 4.1: Rating of the Effect of Interest Rate Capping on Banks

<table>
<thead>
<tr>
<th>Effect of Interest Rate Capping</th>
<th>SD %</th>
<th>D %</th>
<th>N %</th>
<th>A %</th>
<th>SA %</th>
<th>Mean</th>
<th>Std Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate capping has reduced bank profits</td>
<td>2.9</td>
<td>10.3</td>
<td>4.4</td>
<td>22.1</td>
<td>60.3</td>
<td>4.26</td>
<td>1.128</td>
</tr>
<tr>
<td>Interest rate capping has increased risk and operation cost</td>
<td>14.7</td>
<td>14.7</td>
<td>19.1</td>
<td>17.6</td>
<td>33.8</td>
<td>3.41</td>
<td>1.458</td>
</tr>
<tr>
<td>Interest rate capping has increased access to finance to small corporations</td>
<td>27.9</td>
<td>17.6</td>
<td>5.9</td>
<td>16.2</td>
<td>32.4</td>
<td>3.07</td>
<td>1.669</td>
</tr>
<tr>
<td>Interest rate capping has reduced supply of credit</td>
<td>4.4</td>
<td>8.8</td>
<td>4.4</td>
<td>35.3</td>
<td>47.1</td>
<td>4.12</td>
<td>1.127</td>
</tr>
<tr>
<td>Interest rate capping has led to development of new products or services</td>
<td>10.3</td>
<td>7.4</td>
<td>11.8</td>
<td>32.4</td>
<td>38.2</td>
<td>3.81</td>
<td>1.307</td>
</tr>
<tr>
<td>Interest rate capping has placed a strong emphasis on the development of new organizational processes</td>
<td>4.4</td>
<td>13.2</td>
<td>13.2</td>
<td>33.8</td>
<td>35.3</td>
<td>3.82</td>
<td>1.184</td>
</tr>
<tr>
<td>Interest rate capping has introduced many new processes, policies, products, and services</td>
<td>10.3</td>
<td>5.9</td>
<td>7.4</td>
<td>41.2</td>
<td>35.3</td>
<td>3.85</td>
<td>1.261</td>
</tr>
<tr>
<td>Interest rate capping has made changes in processes, policies, products, or services</td>
<td>2.9</td>
<td>11.8</td>
<td>11.8</td>
<td>47.1</td>
<td>26.5</td>
<td>3.82</td>
<td>1.050</td>
</tr>
<tr>
<td>Interest rate capping has increased level of performance on banks</td>
<td>26.9</td>
<td>22.4</td>
<td>20.9</td>
<td>13.4</td>
<td>16.4</td>
<td>2.70</td>
<td>1.425</td>
</tr>
<tr>
<td>Interest rate capping has increased financial risk of banks</td>
<td>8.8</td>
<td>11.8</td>
<td>10.3</td>
<td>44.1</td>
<td>25</td>
<td>3.65</td>
<td>1.231</td>
</tr>
</tbody>
</table>

Interest rate capping has led to development of new products or services as indicated by 70.6% of the respondents who agreed while 17.7% disagreed and 11.8% were neutral with a mean of 3.81 and a standard deviation of 1.307. Interest rate capping has placed a strong emphasis on the development of new organizational processes as indicated by 69.1% of the respondents who agreed while 17.6% disagreed and 13.2% were neutral.
with a mean of 3.82 and a standard deviation of 1.184. Interest rate capping has introduced many new processes, policies, products, and services as indicated by 76.5% of the respondents who agreed while 16.2% disagreed and 7.4% were neutral with a mean of 3.85 and a standard deviation of 1.261.

Interest rate capping has made changes in processes, policies, products, or services as indicated by 73.6% of the respondents who agreed while 14.7% disagreed and 11.8% were neutral with a mean of 3.82 and a standard deviation of 1.050. Interest rate capping has not increased the level of performance on banks as indicated by 49.3% of the respondents who disagreed while 29.8% agreed and 20.9% were neutral with a mean of 2.70 and a standard deviation of 1.425. Interest rate capping has increased financial risk of banks as indicated by 69.1% of the respondents who agreed while 20.6% disagreed and 10.3% were neutral with a mean of 3.65 and a standard deviation of 1.231.

4.3.2 Correlations for Effect of Interest Rate Capping on Commercial Banks
Table 4.2 presents the Pearson correlation results between interest rate cap and its effect on commercial banks. The results show that interest rate cap had a significant effect on commercial banks ($r=0.759$, $p<0.1$).

<table>
<thead>
<tr>
<th>Interest Rate Cap</th>
<th>Pearson Correlation</th>
<th>Sig. (2-tailed)</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td></td>
<td>68</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Effect on Banks</th>
<th>Pearson Correlation</th>
<th>Sig. (2-tailed)</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.759**</td>
<td>.000</td>
<td>68</td>
</tr>
</tbody>
</table>

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

4.3.3 Model Summary for Effect of Interest Rate Capping on Commercial Banks
Table 4.3 presents the regression model results for the relationship between interest rate cap and its effect on commercial banks. The results show that interest rate cap accounted for a 56.9% change in commercial banks.
Table 4.3: Model Summary for Effect of Interest Rate Capping on Banks

<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>.759</td>
<td>.576</td>
<td>.569</td>
<td>.37513</td>
</tr>
</tbody>
</table>

Predictors: (Constant), Effect on Commercial Banks

4.3.4 Regression Coefficient for Effect of Interest Rate Capping on Banks

Table 4.4 presents the regression results for the relationship between interest rate cap and its effect on commercial banks. The results show that interest rate cap had a positive and significant effect on commercial banks and for every single unit increase in interest cap, there would be a 66.7% effect on commercial banks.

Table 4.4: Regression Coefficient for Effect of Interest Rate Capping on Banks

<table>
<thead>
<tr>
<th>Model</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>1</td>
<td>(Constant)</td>
<td>1.543</td>
<td>.667</td>
<td>5.901</td>
</tr>
<tr>
<td></td>
<td>Effect on Banks</td>
<td>1.543</td>
<td>.667</td>
<td>5.901</td>
</tr>
</tbody>
</table>

a. Dependent Variable: Interest Cap

4.4 Challenges of Interest Capping on Commercial Banks

4.4.1 Rating of the Challenges of Interest Capping on Banks

Table 4.5 indicates that interest rate capping has reduced profit margins as shown by 86.7% of the respondents who agreed while 7.4% were neutral and 5.8% disagreed with a mean of 4.31 and a standard deviation of 0.950. Interest rate capping has reduced lending as shown by 85.3% of the respondents who agreed while 8.8% disagreed and 5.9% were neutral with a mean of 4.22 and a standard deviation of 0.912. Interest rate capping has increased layoffs as shown by 69.1% of the respondents who agreed while 17.7% disagreed and 13.2% were neutral with a mean of 3.82 and a standard deviation of 1.360. Interest rate capping has heightened operational cost and risk as shown by 64.7% of the respondents who agreed while 25% were neutral and 10.3% disagreed with a mean of 3.79 and a standard deviation of 0.939.
<table>
<thead>
<tr>
<th></th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate capping has reduced profit margins</td>
<td>2.9</td>
<td>2.9</td>
<td>7.4</td>
<td>33.8</td>
<td>52.9</td>
<td>4.31</td>
<td>.950</td>
</tr>
<tr>
<td>Interest rate capping has reduced lending</td>
<td>0</td>
<td>8.8</td>
<td>5.9</td>
<td>39.7</td>
<td>45.6</td>
<td>4.22</td>
<td>.912</td>
</tr>
<tr>
<td>Interest rate capping has increased layoffs</td>
<td>11.8</td>
<td>5.9</td>
<td>13.2</td>
<td>26.5</td>
<td>42.6</td>
<td>3.82</td>
<td>1.360</td>
</tr>
<tr>
<td>Interest rate capping has heightened operational cost and risk</td>
<td>0</td>
<td>10.3</td>
<td>25</td>
<td>39.7</td>
<td>25</td>
<td>3.79</td>
<td>.939</td>
</tr>
<tr>
<td>Interest rate capping has increased in total cost of loans through additional fees</td>
<td>10.3</td>
<td>17.6</td>
<td>5.9</td>
<td>39.7</td>
<td>26.5</td>
<td>3.54</td>
<td>1.332</td>
</tr>
<tr>
<td>Interest rate capping has increased probability of merger and consolidation for survival</td>
<td>13.2</td>
<td>4.4</td>
<td>32.4</td>
<td>27.9</td>
<td>22.1</td>
<td>3.41</td>
<td>1.261</td>
</tr>
<tr>
<td>Interest rate capping has increased expansion rate</td>
<td>30.9</td>
<td>26.5</td>
<td>23.5</td>
<td>8.8</td>
<td>10.3</td>
<td>2.41</td>
<td>1.296</td>
</tr>
<tr>
<td>Interest rate capping has increased evolving customer needs</td>
<td>5.9</td>
<td>20.6</td>
<td>14.7</td>
<td>36.8</td>
<td>22.1</td>
<td>3.49</td>
<td>1.215</td>
</tr>
<tr>
<td>Interest rate capping has increased compliance with regulatory requirements</td>
<td>2.9</td>
<td>5.9</td>
<td>14.7</td>
<td>36.8</td>
<td>39.7</td>
<td>4.04</td>
<td>1.028</td>
</tr>
<tr>
<td>Interest rate capping has rendered some processes obsolete</td>
<td>4.4</td>
<td>13.2</td>
<td>22.1</td>
<td>29.4</td>
<td>30.9</td>
<td>3.69</td>
<td>1.175</td>
</tr>
</tbody>
</table>

Interest rate capping has increased in total cost of loans through additional fees as shown by 66.2% of the respondents who agreed while 27.9% disagreed and 5.9% were neutral with a mean of 3.54 and a standard deviation of 1.332. Interest rate capping has increased probability of merger and consolidation for survival as shown by 50% of the respondents who agreed while 32.4% were neutral and 17.6% were neutral with a mean of 3.41 and a standard deviation of 1.261. Interest rate capping has not increased expansion rate as
shown by 57.4% of the respondents who disagreed, while 23.5% were neutral and 19.1% agreed with a mean of 2.41 and a standard deviation of 1.296.

Interest rate capping has increased evolving customer needs as shown by 58.9% of the respondents who agreed while 26.5% disagreed and 14.7% were neutral with a mean of 3.49 and a standard deviation of 1.215. Interest rate capping has increased compliance with regulatory requirements as shown by 76.5% of the respondents who agreed while 14.7% were neutral, and 8.8% disagreed with a mean of 4.04 and a standard deviation of 1.028. Interest rate capping has rendered some processes obsolete as shown by 60.3% of the respondents who agreed while 29.4% were neutral, and 17.6% disagreed with a mean of 3.69 and a standard deviation of 1.175.

4.4.2 Correlations for the Challenges of Interest Rate Capping on Banks
Table 4.6 presents the Pearson correlation results between interest cap and the challenges it posed for commercial banks. The results show that interest cap posed a significant challenge on commercial banks (r=0.589, p<0.01).

<table>
<thead>
<tr>
<th>Interest Rate Cap</th>
<th>Pearson Correlation</th>
<th>Sig. (2-tailed)</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>68</td>
</tr>
<tr>
<td>Challenges on Banks</td>
<td>Pearson Correlation</td>
<td>0.589**</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>0.000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>68</td>
<td>68</td>
</tr>
</tbody>
</table>

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

4.4.3 Model Summary for Challenges of Interest Rate Capping on Banks
Table 4.7 presents the regression model results for the relationship between interest rate cap and the challenges posed to commercial banks. The results show that interest rate cap accounted for a 33.7% change in challenges faced by commercial banks.
Table 4.7: Model Summary for Challenges of Interest Rate Capping on Banks

<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>.589</td>
<td>.347</td>
<td>.337</td>
<td>.46517</td>
</tr>
</tbody>
</table>

Predictors: (Constant), Commercial Bank Challenges

4.4.4 Regression Coefficient for Challenges of Interest Rate Capping on Banks

Table 4.8 presents the regression results for the relationship between interest rate cap and the challenges posed to commercial banks. The results show that interest rate cap had a positive and significant effect on the challenges faced by commercial banks and for every single unit increase in interest cap, there would be a 60.7% effect on the challenges faced by commercial banks.

Table 4.8: Regression Coefficient for Challenges of Interest Rate Capping on Banks

<table>
<thead>
<tr>
<th>Model</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>1.748</td>
<td>.381</td>
<td>.381</td>
<td>4.593</td>
</tr>
<tr>
<td>Challenges on Banks</td>
<td>.607</td>
<td>.102</td>
<td>.589</td>
<td>5.927</td>
</tr>
</tbody>
</table>

a. Dependent Variable: Interest Cap

4.5 Strategies Used by Commercial Banks during Interest Rate Capping

4.5.1 Rating of Strategies Used by Commercial Banks during Interest Rate Capping

Table 4.9 shows that the development of new products or services has improved the banks’ competitiveness as indicated by 91.2% of the respondents who agreed while 4.4% equally disagreed and another 4.4% being neutral with a mean of 4.24 and a standard deviation of 0.900. Offering different products to different demographic groups has led to new markets for the banks as indicated by 86.7% of the respondents who agreed while 7.3% disagreed and 5.9% were neutral with a mean of 4.15 and a standard deviation of 0.935. Operational efficiency through system upgrade /change has improved service delivery as indicated by 91.2% of the respondents who agreed while 5.9% were neutral and 3% disagreed with a mean of 4.32 and a standard deviation of 0.781.
Table 4.9: Rating of the Strategies Used by Banks during Interest Rate Capping

<table>
<thead>
<tr>
<th>Strategy Description</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
<th>Mean</th>
<th>Std</th>
</tr>
</thead>
<tbody>
<tr>
<td>The development of new products or services has improved our banks competitiveness</td>
<td>4.4</td>
<td>0</td>
<td>4.4</td>
<td>50</td>
<td>41.2</td>
<td>4.24</td>
<td>.900</td>
</tr>
<tr>
<td>Offering different products to different demographic groups has led to new markets for our bank</td>
<td>2.9</td>
<td>4.4</td>
<td>5.9</td>
<td>48.5</td>
<td>38.2</td>
<td>4.15</td>
<td>.935</td>
</tr>
<tr>
<td>Operational efficiency through system upgrade /change has improved our service delivery</td>
<td>1.5</td>
<td>1.5</td>
<td>5.9</td>
<td>45.6</td>
<td>45.6</td>
<td>4.32</td>
<td>.781</td>
</tr>
<tr>
<td>Servicing a targeted market has ensured customer satisfaction</td>
<td>1.5</td>
<td>0</td>
<td>19.1</td>
<td>41.2</td>
<td>38.2</td>
<td>4.15</td>
<td>.833</td>
</tr>
<tr>
<td>Introducing many new processes, policies, products, and services has improved efficiency</td>
<td>8.8</td>
<td>10.3</td>
<td>13.2</td>
<td>50</td>
<td>17.6</td>
<td>3.57</td>
<td>1.163</td>
</tr>
<tr>
<td>Cost leadership has led to reduced operational cost</td>
<td>2.9</td>
<td>5.9</td>
<td>23.5</td>
<td>35.3</td>
<td>32.4</td>
<td>3.88</td>
<td>1.030</td>
</tr>
<tr>
<td>Enhanced customer care has improved the relationship with our clients</td>
<td>5.9</td>
<td>16.2</td>
<td>13.2</td>
<td>35.3</td>
<td>29.4</td>
<td>3.66</td>
<td>1.229</td>
</tr>
<tr>
<td>Investing in research has led to new markets and improved strategies</td>
<td>4.4</td>
<td>1.5</td>
<td>13.2</td>
<td>44.1</td>
<td>36.8</td>
<td>4.07</td>
<td>.982</td>
</tr>
</tbody>
</table>

Servicing a targeted market has ensured customer satisfaction as indicated by 79.4% of the respondents who agreed while 19.1% were neutral and 1.5% disagreed with a mean of 4.15 and a standard deviation of 0.833. Introducing many new processes, policies, products, and services has improved efficiency as indicated by 67.6% of the respondents who agreed while 19.1% disagreed and 13.2% were neutral with a mean of 3.57 and a standard deviation of 1.163. Cost leadership has led to reduced operational cost as indicated by 67.7% of the respondents who agreed while 23.5% were neutral, and 8.8% disagreed with a mean of 3.88 and a standard deviation of 1.030. Enhanced customer care has improved the relationship with clients as indicated by 64.7% of the respondents who
agreed while 22.1% disagreed and 13.2% were neutral with a mean of 3.66 and a standard deviation of 1.229. Investing in research has led to new markets and improved strategies as indicated by 80.9% of the respondents who agreed while 13.2% were neutral, and 5.9% disagreed with a mean of 4.07 and a standard deviation of 0.982.

### 4.5.2 Correlations for Strategies Used by Banks during Interest Rate Capping

Table 4.10 presents the Pearson correlation results between interest cap and the strategies used by commercial banks. The results show that interest cap resulted in a significant effect on the strategies that were applied by banks ($r=0.578$, $p<0.01$).

<table>
<thead>
<tr>
<th>Interest Rate Cap</th>
<th>Bank Strategies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pearson Correlation</td>
<td>1.000</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>68</td>
</tr>
<tr>
<td>Bank Strategies</td>
<td>Pearson Correlation</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>0.000</td>
</tr>
<tr>
<td>N</td>
<td>68</td>
</tr>
</tbody>
</table>

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

### 4.5.3 Model Summary for Strategies Used by Banks during Interest Rate Capping

Table 4.11 presents the regression model results for the relationship between interest rate cap and the strategies employed by commercial banks. The results show that interest rate cap accounted for a 32.3% change in strategies employed by commercial banks.

<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>.578</td>
<td>.334</td>
<td>.323</td>
<td>.47008</td>
</tr>
</tbody>
</table>

Predictors: (Constant), Strategies Used by Commercial Banks
4.4.4 Regression Coefficient for Challenges of Interest Rate Capping on Banks

Table 4.12 presents the regression results for the relationship between interest rate cap and the strategies used by commercial banks. The results show that interest rate cap had a positive and significant effect on the strategies employed by commercial banks and for every single unit increase in interest cap, there would be a 54.3% effect on the strategies employed by commercial banks.

Table 4.12: Regression Coefficient for Strategies Used by Banks during Interest Rate Capping

<table>
<thead>
<tr>
<th>Model</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>1 (Constant)</td>
<td>1.806</td>
<td>.382</td>
<td>.382</td>
<td>4.722</td>
</tr>
<tr>
<td>Bank Strategies</td>
<td>.543</td>
<td>.094</td>
<td>.578</td>
<td>5.747</td>
</tr>
</tbody>
</table>

a. Dependent Variable: Interest Cap

4.6 Chapter Summary

This chapter has looked at the analysis of the data collected from various banks. An analysis of the collected data was carried out using SPSS software and Microsoft Excel. The results were presented in form of figures and tables for ease of analysis. The data collected and analyzed helped in getting answers to the research objectives that were posed in chapter one and in chapter five, discussions and conclusions on the findings were be discussed.
CHAPTER FIVE
5.0 DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction
This chapter endeavors to delineate usefulness and applicability of the research. The chapter provides a summary of the study findings, as well as a detailed discussion of the findings. The chapter provides the study’s conclusions and also offers recommendations based on the study findings.

5.2 Summary
The general objective of this study was to assess interest rate capping on commercial banks in Kenya. The study sought to determine the effect of interest rate capping of the competitiveness of banks in Kenya, assess the challenges posed to commercial banks by interest rate capping regulation, and to determine the strategies employed by commercial banks during interest rate capping.

The study adopted a cross-sectional survey design. This design method was selected on the basis that it can collect diverse information types and is quick and less costly. The population of interest this research study comprised of top and middle marketing managers from tier 1 Commercial Banks within Nairobi County who were 240. The sampling frame of the study consisted of the list of branch managers and was obtained from the Central Bank report. The sampling embraced a mixed method approach to sampling techniques involving stratified sampling technique and simple random sampling (SRS). The sample size was determined using the Yamane formula which gave the study a sample size of 68 managers. This study applied questionnaires collected from respondents as primary data which was analyzed quantitatively. The data was analyzed using descriptive statistics and inferential statistics. These were presented using tables and figures.

The study showed that interest rate capping has reduced bank profits and increased risk and operational cost for commercial banks. Interest rate capping has also increased access to finance to small corporations at the same time, it has reduced supply of credit. The study revealed that interest rate capping has led to development of new products or services in Kenyan commercial banks, and it has placed a strong emphasis on the development of new organizational processes, policies, products, and services. The study
also indicated that interest rate capping has not increased the level of performance of banks because it has increased financial risk of these banks.

The study revealed that interest rate capping has reduced profit margins and lending for Kenyan commercial banks. This has led to an increase in employee layoffs as well as heightening the operational cost and risk. Interest rate capping has increased in total cost of loans through additional fees which has led to an increase in probability of mergers and consolidation for bank survival. The study showed that interest rate capping has not increased the expansion rate of commercial banks in Kenya, but instead, it has increased the evolving customer needs and the compliance of commercial banks with regulatory requirements since capping has rendered some processes obsolete.

The study indicated that the development of new products or services has improved the banks’ competitiveness in the Kenyan market and the fact that banks are offering different products to different demographic groups has led to new markets for the banks. Interest capping has increased the operational efficiency through system upgrades which has ultimately improved service delivery of commercial banks. The study showed that servicing a targeted market has ensured customer satisfaction and the introduction of many new processes, policies, products, and services has improved efficiency. The study revealed that cost leadership has led to reduced operational cost, and enhanced customer care has improved the relationship between commercial banks and clients. The study also indicated that investing in research by commercial banks in Kenya has led to new markets and improved strategies.

5.3 Discussions

5.3.1 Effect of Interest Rate Capping on Commercial Banks

Interest rate capping has reduced bank profits. These findings correlate with those of Aren and Duhn (2016), that, interest rates have an effect on profits of banks directly. Hurn and Farl (2007) state that, interest rates have an effect on bank gain either directly or indirectly.

Interest rate capping has increased risk and operation cost. Similar observations were made by Osei-Assibey and Bockarie (2013) who note that, interest rate capping slows down the flow of credit to some specific sectors perceived to be riskier and leads to
increased transaction fees and commissions charged to compensate for the expected decreased in earnings.

Interest rate capping has increased access to finance to small corporations. These observations differ from those of Rosenberg et al. (2009) who notes that, because of interest rate capping, banks have less appetite to supply unsecured to individuals or organizations including Small and Medium Enterprises (SMEs) perceived to be more risky.

Interest rate capping has reduced supply of credit. This is confirmed by Edris (1997) who observed that, with the emergence of interest rate capping, banks are unable to maintain an economic interest rate spread and thus they are exposed to credit risk and at last this leads to reduction of profits.

Interest rate capping has led to development of new products or services. These observations differ from those of Ngai et al. (2016) who noted that, coming from a highly regulated regime, banks in China generally lacked capabilities for determining exact baseline costs for individual products, and as a result had trouble establishing crucial metrics such as funds transfer pricing, risk, economic capital, and cost allocation.

Interest rate capping has placed a strong emphasis on the development of new organizational processes. Similar findings were supported by Zhang et al. (2016) who state that adopting modern pricing processes can deliver a significant boost in revenues, provide improved services for the dominant corporate banking segment, and support management performance improvements in the mid- and back offices.

Interest rate capping has introduced many new processes, and has changed policies, products, and services. The results coincide with those of Faizan (2016) who dispensed a study to analyze the impact of economic reforms, monetary easing and banking regulation and policies focusing on seventy-six economies and concluded that monetary reform and specifically interest rate capping had a negative and statistically vital impact on bank interest margins.
Interest rate capping has not increased the level of performance on banks. Similar results were noted by Priti (2016) who stated that, the performance of commercial banks depends on a wide range of business, but interest rates still play a key role in determining the financial performance and the effective competitive strategies to be employed.

Interest rate capping has increased financial risk of banks. This is confirmed by Edris (1997) who observed that, with the emergence of interest rate capping, banks are unable to maintain an economic interest rate spread and thus they are exposed to credit risk and at last this leads to reduction of profits.

5.3.2 Challenges of Interest Capping on Commercial Banks
Interest rate capping has reduced profit margins. These observations concurs with those of Rug (2013), that profitability and monetary performance is measured by how well the management uses company’s assets to come up with profits, and Teern (2011) also states that, conversely, redoubled interest rates discourage shoppers from borrowing and this results in reduced interest financial gain generated and successively reduced profits of the bank.

Interest rate capping has reduced lending. Similar observations were made by Acquaah and Yasai-Ardekani (2008) in China, and observed that, the government supports the financial sector by setting a ceiling on deposits and a floor on lending rates meaning that banks are able to sustain a minimum level of margin.

Interest rate capping has increased layoffs. Similar observations were made by Stevenson (2016) in a research in German and Great Britain banks where his study revealed that the changes on the capping law and banking rules reshaped German and Great Britain banking establishments, and bank staffs were facing an ever-increasing pressure as their employers attempt to become economical, streamlining banks with a high orientation towards their shareholders during an extremely competitive market.

Interest rate capping has heightened operational cost and risk. These findings correlate with those of Porter (2014), that competitive advantages are attributed to a variety of factors, including cost structure, brand and quality of product offerings, distribution network, intellectual property and customer support.
Interest rate capping has increased in total cost of loans through additional fees. These results coincide with Central Bank annual report (2015) that, before interest rates were capped the interest rate on loans, deposit and mortgages were being determined by the banks individually. The interest rates were very high and the banks were performing very well.

Interest rate capping has increased probability of merger and consolidation for survival. The results are similar to those of Wheelock and Wilson (2004) who found that expected merger activity in United States (US) banking is positively related to management rating, bank size, competitive position and geographical location of banks and negatively related to market concentration.

Interest rate capping has not increased expansion rate. These study results differ with that of Marciukaiyte et al. (2009) who state that, compared with M&A or formations of joint venture, strategic alliance is a relatively flexible and easy operated approach for inter-firm collaboration to seize the growth opportunity.

Interest rate capping has increased evolving customer needs. Similar observations were made by Shammot (2011) who state that, product differentiation strategy can be a tool of competitive advantage which is adopted by organizations to provide products that satisfies individual customer’s needs. In satisfying individual customer’s needs, quality has become a major differentiating factor among products.

Interest rate capping has increased compliance with regulatory requirements. Ekpu and Paloni (2016) noted that, to truly bring down interest rates sustainably, governments need to build a business and regulatory environment and support structures that encourage the supply of financial services at lower cost and hence push the supply curve to the right.

Interest rate capping has rendered some processes obsolete. This is confirmed by Bauer and Colgan (2001) who observed that, lower costs and cost advantages result from learning curve benefits, economies of scale, process innovations, product designs, reengineering activities and reducing manufacturing time and costs.
5.3.3 Strategies Used by Commercial Banks during Interest Rate Capping
The development of new products or services has improved the banks’ competitiveness. Helms et al. (2007) echoes the same results that, by producing high qualified and standardize products or services, at the same time, with the effects of the economic scale and experience curve, the firm strives to gain a sustainable competitive advantage among its competitors.

Offering different products to different demographic groups has led to new markets for the banks. Similar findings were supported by Zhang et al. (2016) who state that adopting modern pricing processes can deliver a significant boost in revenues, provide improved services for the dominant corporate banking segment, and support management performance improvements in the mid- and back offices.

Operational efficiency through system upgrade/change has improved service delivery. Helms et al. (2007) echoes the same results that, by producing high qualified and standardize products or services, at the same time, with the effects of the economic scale and experience curve, the firm strives to gain a sustainable competitive advantage among its competitors.

Servicing a targeted market has ensured customer satisfaction. Similar observations were made by Shammot (2011) who state that, product differentiation strategy can be a tool of competitive advantage which is adopted by organizations to provide products that satisfies individual customer’s needs. In satisfying individual customer’s needs, quality has become a major differentiating factor among products.

Introducing many new processes, policies, products, and services has improved efficiency. Landerman (2000) states that, the evidence suggests that learning by doing is a key factor in building up efficiency and hence lowering overheads and hence interest rates. Institutions with a decent track record are better able to control costs and more efficient at evaluating loans while a larger loan book will generate economies of scale.

Cost leadership has led to reduced operational cost. Comparable observations are made by Cole (2008), that successful implementation of the differentiation strategy requires resources and skills. Firms that implement a cost leadership strategy are able to secure a
relatively large market share by being the lowest cost producers or service providers in their industry or market. Ramsey (2013) adds that, firms implementing the cost leadership strategy can obtain above-normal profits because of their ability to lower prices to match or even below those of competitors and still earn profits.

Enhanced customer care has improved the relationship with clients. Zhang et al. (2016) also notes that, planning a strategy around each major corporate account requires collaboration among relationship managers, team leaders, product managers, and risk managers. The result is a product package designed for individual corporate needs, a level of attention that can create closer relationships. In addition, sophisticated pricing systems not only suggest optimal prices, but also identify potential cross-selling opportunities.

Investing in research has led to new markets and improved strategies. Bikker (2003) also stated that, competition in the banking sector has been analyzed by measuring market power, that is, a reduction in competitive pressure and efficiency. A well-known approach to measuring market power.

5.4 Conclusions

5.4.1 Effect of Interest Rate Capping on Commercial Banks
The study concludes that interest rate capping has reduced bank profits and increased risk and operational cost for commercial banks. Interest rate capping has also increased access to finance to small corporations at the same time, it has reduced supply of credit. The study concludes that interest rate capping has led to development of new products or services in Kenyan commercial banks, and it has placed a strong emphasis on the development of new organizational processes, policies, products, and services. The study also concludes that interest rate capping has not increased the level of performance of banks because it has increased financial risk of these banks.

5.4.2 Challenges of Interest Capping on Commercial Banks
The study concludes that interest rate capping has reduced profit margins and lending for Kenyan commercial banks. This has led to an increase in employee layoffs as well as heightening the operational cost and risk. Interest rate capping has increased in total cost of loans through additional fees which has led to an increase in probability of mergers and consolidation for bank survival. The study concludes that interest rate capping has not
increased the expansion rate of commercial banks in Kenya, but instead, it has increased the evolving customer needs and the compliance of commercial banks with regulatory requirements since capping has rendered some processes obsolete.

5.4.3 Strategies Used by Commercial Banks during Interest Rate Capping
The study concludes that the development of new products or services has improved the banks’ competitiveness in the Kenyan market and the fact that banks are offering different products to different demographic groups has led to new markets for the banks. Interest capping has increased the operational efficiency through system upgrades which has ultimately improved service delivery of commercial banks. The study concludes that servicing a targeted market has ensured customer satisfaction and the introduction of many new processes, policies, products, and services has improved efficiency. The study concludes that cost leadership has led to reduced operational cost, and enhanced customer care has improved the relationship between commercial banks and clients. The study also concludes that investing in research by commercial banks in Kenya has led to new markets and improved strategies.

5.5 Recommendations
5.5.1 Recommendations for Improvement
5.5.1.1 Effect of Interest Rate Capping on Commercial Banks
The study recommends that the regulators review for indirect alternatives for helping the public access credit as opposed to using the interest rate capping method. This is because the interest rate capping law has created high financing costs charged by banks which ultimately led to diminished access to credit that is essential for impelling monetary development.

5.5.1.2 Challenges of Interest Capping on Commercial Banks
The study recommends arrangement creators in this manner should re-examine the impact of the interest rate capping law and consider letting the market structure and credit risk play a major role. This is on account of banks fixing the loaning criteria given that they were not any more ready to remunerate danger of default by differing advance evaluating to coordinate the hazard accepted starting with one credit ask for them onto the next.
5.5.1.3 Strategies Used by Commercial Banks during Interest Rate Capping

The study recommends that bank managers make use of various available strategies to ensure their performance is not highly impacted by the interest cap. Since banks give money related administrations to make benefits, interest rate capping law will negatively affected bank productivity and profitability, and hence the need to adopt better strategies.

5.5.2 Recommendation for Further Studies

This study recommends that a study on success factors for gaining competitive advantage by commercial banks in this era of interest rate capping be conducted to facilitate better positioning of commercial banks in Kenya. This research will demystify the competitive strategies adopted by commercial banks and unravel other possible incomes for these financial institutions other than the current near overdependence on interest income. Further studies that will covering extra banks also ought to be conducted in an attempt to completely comprehend the effect of interest capping in Kenya.
REFERENCES


APPENDICES
APPENDIX I: COVER LETTER

United States International University – Africa,
P.O. Box 14634 – 00800,
Nairobi – Kenya.

Dear Respondent,

REF: REQUEST TO PARTICIPATE IN THIS RESEARCH.
Dear respondent, I am a Master’s student at the United States International University – Africa, and in order for me to graduate, I am required to carry out a study research that aims to assess interest rate capping on commercial banks in Kenya.

This study is aimed at studying all Tier 1 Banks in Kenya, and thus your organization is among those selected. Do note that, before this exercise begins, clearance has been sought from your bank managers, and thus you are free to provide the researcher with the required information. If you so wish, you may take the questionnaire home, and fill at your convenience.

All the information that will be collected in this exercise will be treated with utmost confidentiality. Collected information will solely be for academic purposes.

Yours Sincerely,

Godfrey Mutinda Peter.
APPENDIX II: QUESTIONNAIRE

PART A: BACKGROUND INFORMATION

1. Gender
Male [   ]    Female [   ]

2. Age
Below 30 [   ]  31-40 [   ]  41-50 [   ]  51-60 [   ]  Above 60 [   ]

3. What is your job level?
Top management [   ]    Middle Management [   ]

4. How long has your bank been in Kenya?
Below 1 year [   ]  2-5 years [   ]  6-10 years [   ]
11-15 years [   ]  16-19 years [   ]  20 and above [   ]

5. Using the categories below, please indicate the size of your bank in regards to capital base
1 Billion - 5 Billion [   ]  6 Billion -10 Billion [   ]  11 Billion – 15 Billion [   ]
Over 16 Billion [   ]

6) Kindly indicate the size of your bank with regards to number of employees
Below 500 [   ]  Between 500-1000 [   ]  Between 1000-3000 [   ]
Between 3000-5000 [   ]  Over 5000 [   ]
PART B: TO WHAT EXTENT HAS INTEREST RATE CAPPING AFFECTED THE FOLLOWING ASPECTS IN YOUR BANK?

7. Please tick one box on each line. (1) Strongly disagree (2) Disagree (3) Neutral (4) Agree (5) strongly agree

<table>
<thead>
<tr>
<th>aspect</th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate capping has reduced bank profits</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased risk and operation cost</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased access to finance to small corporations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has reduced supply of credit</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has led to development of new products or services</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has placed a strong emphasis on the development of new organizational processes</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has introduced many new processes, policies, products, and services.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has made changes in processes, policies, products, or services.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased level of performance on banks</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased financial risk of banks</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**PART C: TO WHAT EXTENT HAS YOUR BANK FACED THE FOLLOWING CHALLENGES DUE TO INTEREST RATE CAPPING?**

Please tick one box on each line. (1) Strongly disagree (2) Disagree (3) Neutral (4) Agree (5) strongly agree

<table>
<thead>
<tr>
<th></th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate capping has reduced profit margins</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has reduced lending</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased layoffs</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has heightened operational cost</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>and risk</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased in total cost of loans</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>through additional fees</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased probability of</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>merger and consolidation for survival</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased expansion rate</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased evolving customer needs</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has increased compliance with regulatory requirements</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest rate capping has rendered some processes obsolete</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
D: TO WHAT EXTENT HAVE THE FOLLOWING STRATEGIES IMPROVED YOUR BANKS COMPETETIVENESS?
(1) Strongly disagree (2) Disagree (3) Neutral (4) Agree (5) strongly agree Please tick one box on each line.

<table>
<thead>
<tr>
<th></th>
<th>SD</th>
<th>D</th>
<th>N</th>
<th>A</th>
<th>SA</th>
</tr>
</thead>
<tbody>
<tr>
<td>The development of new products or services has improved our banks competitiveness</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Offering different products to different demographic groups has led to new markets for our bank</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Operational efficiency through system upgrade/change has improved our service delivery</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Servicing a targeted market has ensured customer satisfaction</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Introducing many new processes, policies, products, and services has improved efficiency</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Cost leadership has led to reduced operational cost</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Enhanced customer care has improved the relationship with our clients</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Investing in research has led to new markets and improved strategies</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
</tbody>
</table>

THE END