Original Article

Relationship between Strategic Product Innovation and Growth of Commercial Banks in Kenya

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ABSTRACT

The growth of commercial banks is pegged on; asset quality, amount of loans disbursed, number of customers (with accounts), loan repayment rate, quantity of deposits, profitability and also branch network. However, in recent years, the banking sector has consistently been characterized by growth challenges leading to the closure of bank branches, downsizing operations and fluctuation in non-performing loans. The relationship between product innovations and the growth of commercial banks in Kenya has not yet been adequately studied. The purpose of this research was to establish how product innovation strategy affected the growth of commercial banks in Kenya. The study adopted descriptive survey design with the target population consisting of all (39) commercial banks in the country. Representatives of 39 commercial banks were selected to participate in the study as respondents since they were not sampled. Data was collected using questionnaire which was tested for validity and reliability prior to administration to the field. Data was subjected to both descriptive and inferential statistical methods with the help of SPSS software. The study found out that product innovation was a strategy that was regularly undertaken by commercial banks in Kenya. The study found that banks have started offering mobile banking products considering that majority of population and the country is connected with mobile and internet network. Karl Pearson correlation showed that there existed significant positive effect of product innovation and commercial banks growth in Kenya ($p<0.05$). This means that through commercial banks innovating through release of various products that meets their customer needs, they attain their growth targets. The study recommends that commercial banks should conduct customer services before launching new products and customers should receive real-time updates with respect to changes or improvements in banks product offering.

APA CITATION

INTRODUCTION

The growth of commercial banks is one of the key focuses that managers, shareholders and stakeholders are concerned with in today's business environment (Nwankpa, 2017). Okeke and Ezeala (2023) noted that amidst competition banks need to grow for continued performance, profitability, stability and sustainability. Some of the growth indicators for commercial banks include an increase in customer base, revenue, number of employees, number of branches, and profitability (Mburu, Munga & Nzili, 2021). The indicators are given different measure of strengths in different commercial banks (Woo, 2017). Whereas a bank would boast of increased in customers deposits, another bank would boast in the numbers of branches they are opening, another bank would report in the increase in loan book while another would pride itself in the reduction of non-performing loans, all these are indicators of financial performance of commercial banks. Issak and Odollo (2023) noted that the number of branches a bank has, implies the growth and expansion of a bank. Nevertheless, the growth of various commercial banks in Kenya has not been smooth and therefore research was carried out to determine whether commercial banks have adopted various strategic innovation practices.

Strategic product innovation is on the forefront in both emergent and advanced economies, in the global competition for talent, resources and market share (Glushchenko, et al., 2019). Stiff competition among commercial banks has left some of them with no option but to find ways to attain competitive advantage through innovation (Nwankpa, 2017). Commercial banks competitiveness globally is determined by the ability and capability to meet the dynamic needs of customers (Zhao, et al., 2019). In addition to products and services designed to meet their needs, today's demanding consumers are more informed, connected and keen to buy products and services that are of high quality, are dependable and have competitive prices (Ibrahim, 2016). The firm with a capacity to innovate is in a better position to compete in markets than one which lacks the innovative ability (Milutinovic, Stosic, & Mihic, 2015). This study therefore looked at the relationship between product innovation and growth of commercial banks in Kenya.

Product innovations include the introduction of new credit, deposit, insurance, leasing, hire purchase, and other financial products (Idah et al, 2023). Product innovations are introduced to respond better to changes in market demand or to improve the efficiency of services that are offered by commercial banks (Zhao, Tsai, & Wang, 2019). Other innovations in banking and financial sector are RTGS, EFT, ACH, MICR, Retail Banking free advisory services, implementation of standing instructions of customers, payments of utility bills, fund transfers, internet banking, telephone banking,

mobile banking, selling insurance products, issue of free cheque books, travellers cheques and many more value-added services across the same industry or to compare industries or sectors in aggregation (Nyamao, & Tari, 2023). Kanyuga (2019) observed that the result of growth of Safaricom in the Kenya telecoms sector was as a result of adoption of process innovative strategies. Ashiru et al. (2023) found out that strategic product innovation is one of the important factors affecting growth and performance of firms across the world.

Therefore, for commercial banks to experience growth, strategic innovation components have to be taken into consideration. Commercial banks in Kenya operate in a highly regulated environment by the Central Bank of Kenya. This means that for banks to remain competitive, they need to be on a continuous change mode, adaptable to changes in the sector and foster innovation for improved growth (Dogan, 2017). It is therefore against this background that commercial banks have realized that strategic innovation is essential for their growth performance, survival and sustenance (Agolla, Makara & Monametsi, 2018). This study therefore examined the relationship between strategic product innovation and growth of commercial banks in Kenya.

Statement of the Problem

Growth is an important indicator of well thriving commercial banks (Nwankpa, 2017). Commercial banks with good innovative strategies always thrive and grow faster than those with poor strategic innovation strategies or those with no innovative strategy at all (Idah, 2023). This shows the importance of commercial banks having embraced strategic product innovation in their operations. The growth of commercial banks is an issue facing the industry in recent times leading to some closing their branches while others initiate retrenchment processes to cut operational costs (CBK, 2022). Research conducted in the banking sector has mostly focused on financial performance (return on equity and return on assets) with minimal focus on other growth indicators of commercial banks (including non-financial ones). This paper therefore looks at how strategic product innovation affects the growth of commercial banks in the country, Kenya.

Literature Review

This section presents the empirical review of research studies that have been undertaken with respect to the relationship between product innovation strategies and growth of commercial banks from different fronts. Several research have been conducted in relation to how product innovation affects growth of organizations especially commercial banks. A study by Kashmari, Nejad and Nayebyazdi (2016) examined the influence of financial product innovation on the share of each bank in attaining deposits (an indicator of growth) in Iran. In terms of methodology, secondary data was collected from 23 banks from the period 2007-2013. The study concluded that the SWIFT system, Point of Sale terminal, mobile banking, ATM machines, and personal identification number (PIN), and other banking facilities provided by each bank, showed that a causal relation in improving the share was caused by innovation. A bilateral relation among the share of deposits and facilities provided by the bank was also found. The gap created from Kashmari et al. (2016) research is that they collected secondary data whereas this study used both primary set of data. Further, Nwankpa (2017) explored the effect of variables of innovation strategy which include product innovation, process innovation, marketing innovation, organisational innovation on variables of organisational performance which consists of product performance, return on equity, market orientation and return on investment in Nigeria. Descriptive survey research design was adopted for the study. The population of the study consists of management staff at the strategic and operational management level from five selected deposit money banks in Lagos State. Product innovation was found to have a significant effect on product performance and this relationship was statistically significant.

The gap created in this research is that it was conducted among Nigerian deposit money banks whereas this study focused on commercial banks that provide more than deposit-taking services.

Another research was conducted by Osei Yunfei, Appienti and Forkuoh (2016) to establish the relationship between product innovation and SMEs Performance in the Manufacturing Sector of Ghana. The aim of the study was to establish the contribution of product innovation to the performance and growth of SMEs in Ghana. The study adopted quantitative approach using survey techniques to gather data from 400 SME owner-managers in Ghana. The study results indicated that SMEs in the cities and with educated entrepreneurs were adopting product innovation at the expense of those in the rural areas. This research departs from Osei et al. (2016) by focusing on banks rather than SMEs. In Kenya, Ibrahim (2016) conducted a study on product innovation in Islamic banking and growth of SMEs in Nairobi. The study adopted an exploratory research design, the target Population was all banks in Kenya that offer Islamic products. The study findings indicated that there was positive and significant relationship between product innovation in Islamic banks and the growth of SMEs in Nairobi. The study pointed out that there was an improvement in response time to customer queries, research and development expenses was included in the budget, and the use of flexible regulations had developed Islamic banking. The gap created by Ibrahim's research is that it focused on religious-aligned banks whereas this study was across all commercial banks as rules and strategies operations are different.

An investigation by Muchemi and Moronge (2017) determined the effect of product innovation strategies on the performance of commercial banks in Kenya. The target population for the study was the staff at the Equity bank group headquarters, with a population of 160 employees. The determined sample size was 115 respondents out of a target population of 160. Findings revealed that product innovation strategies collectively explain variations in performance. The gap created from this study is that it focused on one commercial bank whereas the current study captured all commercial banks in the country. Kanyuga (2019) sought to establish the Influence of Strategic Innovation on Performance of Safaricom Company. The researcher used a desk study review methodology where relevant empirical literature was reviewed to identify main themes. A critical review of empirical literature was conducted to establish the Influence of Strategic Innovation on Performance of Telecommunication Firms in Kenya.

The results from the reviewed literature affirm that, product development had a significant predictive influence on performance in terms of capacity utilization specifically when developing new products while improvement of existing products was found to have no statistically significant influence on performance Safaricom. The gap created here is that Safaricom Company was a telecommunication company whereas this study looks at commercial banks. Idah, Nelima, Odero and Rutto (2023) examined the influence of product innovation on the competitiveness of commercial banks in Kenya. Correlational and descriptive designs were used in targeting 175 general managers and directors of tier 1 commercial banks. It was established that product innovation had significant positive influence on the competitiveness of tier I commercial banks. The study by Idah et al. dependent measure was competitiveness while the present study was on commercial bank growth. The review of studies has shown that product innovation is key to growth and performance of commercial banks. However, none of the studies reviewed have looked at the extent to which commercial banks innovation practices affect their growth in Kenya.

Materials and Methods

This study was guided by descriptive survey research design which allows collection of data to answer research objectives and test hypotheses (Creswell & Creswell, 2019). The target population

for this investigation comprises of all 39 commercial banks in Kenya based on data from Central Bank of Kenya on the Bank Annual Supervision 2022 report. The study collected information from management representatives from the 39 commercial banks together with CBK 2022 annual supervision reports showing commercial banks growth indicators. Considering the target respondents for this study are 39, a sample size was not undertaken since they were all reachable. Therefore, all commercial banks in the country were studied where the researcher visited the commercial banks headquarters and sought permission to administer the research questionnaire to commercial banks management representatives. The data collection instrument to be used in this study was a questionnaire and secondary data from CBK annual supervision reports. Data collected from questionnaire and secondary data collection sheet was analysed using quantitative methods. Data was coded and entered into electronic spread sheets with the use of Statistical Product and Service Solution (SPSS Version 25.0). Thereafter analysis was performed by running descriptive and inferential statistics. Descriptive statistics to be used included; frequencies, percentages, means, median and standard deviations. Inferential statistics used included correlations and linear regression to test the research hypothesis. The probability level was set at 95.0% confidence level.

Results and Discussions

Out of 39 questionnaires issued, only 37 were returned signifying a 94.8% response rate that was found to be adequate in descriptive survey research studies by Mugenda and Mugenda (2019). The respondents were asked to indicate the extent to which customers in their banks utilised various products on the following scale: never (1), rarely (2), sometimes (3), often (4) and always (5). The results of analysis are presented in Table 1.

Table 1: Product innovation by commercial banks in Kenya

Product innovation	R	S	O	A	M	SDv
Application for various flexible local products	2 (5.4%)	18 (48.6%)	11 (29.7%)	6 (16.2%)	3.5676	.8347
Use of RTGs to make money transactions	2 (5.4%)	6 (16.2%)	21 (56.8%)	8 (21.6%)	3.9459	.7798
Application and use of flexible mortgage products	10 (27.0%)	17 (45.9%)	6 (16.2%)	4 (10.8%)	3.1081	.9364
Interbank transfers	2 (5.4%)	14 (37.8%)	13 (35.1%)	8 (21.6%)	3.7297	.8708
Mobile / Online banking products	0 (0.0%)	4 (10.8%)	15 (40.5%)	18 (48.6%)	4.3784	.6812
Global trade services using credit cards	10 (27.0%)	12 (32.4%)	11 (29.7%)	4 (10.8%)	3.2432	.9833
Composite scores					3.6622	0.8477

Key: R-Rarely, S-Sometimes, O-Often, A-Always, M-Mean & SDv-Standard Deviation
Source: Field Data (2023)

Result in Table 1 reveal that sometimes 18 (48.6%) customers of commercial banks use applications for various flexible local products and 11 (29.7%) said that they often use. This means that customers of various banks enjoy various flexible local products availed to them by their financial institutions. Secondly, 21 (6.8%) of respondents indicated that their customers often use RTGs in making huge money transactions above Kshs. 1,000,000/= as per CBK guidelines. Thirdly, 17 (45.9%) mentioned that sometimes 17 (45.9%) their customers apply for various flexible mortgage products. This means that application and use of flexible mortgage products is at average considering that not all banks have designed various mortgage products for their customers.

With respect to inter-bank transfers, 14 (37.8%) said that it happens occasionally, 13 (35.1%) indicated that it often happens, and 8 (21.6%) said that it always happens. The above findings confirm an increase in the usage of inter-bank transfers systems by customers from one bank to another. This is mainly facilitated by Pesapal payment system which allows customers to transfer money from one bank account to another without physically visiting the bank. Findings also show that 15 (40.5%) of customers often use mobile and online banking products while 18 (48.6%) of respondents said that their customers always use mobile and online banking products. This finding demonstrates that more than half of the customers of commercial banks in the country have embraced mobile and online banking products because of their convenience, effectiveness and promptness when making transactions. The finding is similar to Idah (2023) who found out that customers were trained on how to utilise internet and mobile banking products before they were on boarded on the platforms.

On the usage of credit cards when making global trade services by customers of commercial banks,

10 (27.0%) said that their customers rarely use, 12 (32.4%) of customers sometimes use, 11 (29.7%) of customers often use those products while only 11 (29.7%) admitted that their customers used these products. The mean result (M=3.24, SDv=0.98) suggests that the usage of credit cards by commercial banks customers in conducting global trade services was found to be at average level. This could be due to the fact that some customers are not involved in business involving outside the country and therefore cannot use the products designed and developed by banks for such services. Composite values shows that product innovation level was high (M=3.66, SDv=0.84) among commercial banks in the country. This means that commercial banks in the country are continuously innovating new products to ensure effective and efficient banking services delivery to their customers in Kenya.

To establish the effect of product innovation and growth of commercial banks in Kenya, a Karl Pearson correlation was computed based on composite values of product innovation against similar for growth. Results are provided in Table 2.

Table 2 Effect of product innovation on growth of commercial banks in Kenya

		Product innovation	Commercial Banks Growth
Product innovation	Pearson Correlation	1	.535**
	Sig. (2-tailed)		.001
	N	37	37
Commercial Banks Growth	Pearson Correlation	.535**	1
	Sig. (2-tailed)	.001	
	N	37	37
**. Correlation is significant at the 0.01 level (2-tailed).			

Source: Field Data (2023)

Karl Pearson correlation statistics reveal that there exists significant positive relationship (*r*=0.535, *p*=0.001) between product innovation and commercial banks growth in Kenya. The statistics tentatively implies that there is high likelihood that increases in product innovation processes would enhance growth of commercial banks in the country. This is supported by Nyamao and Tari (2023) who

discovered a significant positive effect of product innovation on performance of Fintech firms in Kenya. This means that an increased in product innovation will result to improve in the growth of organisations like customers increase, and market share.

Further a linear regression analysis was computed to establish the overall coefficient and significance of

the relationship between product innovation strategy and commercial bank growth. Model results are provided in Table 3.

Table 3 Model Summary of product innovation and commercial bank growth

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.535[a]	.286	.266	.41444	.286	14.029	1	35	.001
a. Predictors: (Constant), Product innovation									

Source: Field Data (2023)

The correlation coefficient R is 0.535 with an R square of 0.286 that implies that 28.6% of change in growth in commercial banks is explained by the product innovation. Further, the change statistics suggest that the relationship between product innovations on commercial bank growth is linear. Table 4 shows the coefficient table for the above model.

Table 4 Coefficients[a] of product innovation and commercial bank growth

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
1 (Constant)	2.159	.382		5.647	.000
Product innovation	.384	.103	.535	3.745	.001
a. Dependent Variable: Commercial Banks Growth					

Source: Field Data (2023)

The linear model equation can be written as:

$$CBGr = 2.159 + 0.384PRODi$$

The linear regression model shows that there exists significant relationship between product innovation and growth of commercial banks. The statistics suggests that a unit change in product innovation results to growth of commercial banks changing by 0.384. The finding agrees with Kariuki (2017) who found out that through product innovation, commercial banks increased their market share hence growth. Nyamao and Tari (2023) also found out that for companies to growth, they needed to improve on their products and services in order to conform to the changing customers' needs.

Conclusions and Recommendations

Product innovation was found to be a common practice that commercial banks in Kenya were focusing on. Commercial banks management have

introduced various products based on the market trends and demands from their customers. For example, the banks have introduced various applications that enable customers to receive flexible loans, mortgage facilities, undertake inter-bank transfers, use RTGS for large cash transactions, utilise global credit cards and access banking products through mobile and online means. The adoption of product innovation varied from one bank to another based on the banks size (tier), categories of customers and institutions that they served in addition to the strategic goal of the bank towards their customers. The continuous process of product innovation by commercial banks increased their growth indices. Through Kenya Bankers Association, all banks have embedded Pesapal in their systems which brings comprehensive list of services that customers can pay for with a lot of ease from their mobile phones to the banks that they do not own accounts. In general. It was found out that

there was significant relationship between process innovation strategies and growth of commercial banks in Kenya. To ensure successful products are launched, it is important that commercial banks in the country regularly seek customer views or conduct independent surveys before making decisions on development of new products and services. This action will ensure that the products developed are well received and would have significant positive impact on banks growth.

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