OPERATIONAL RISK MANAGEMENT AND COMPETITIVE ADVANTAGE IN THE GHANAIAN BANKING INDUSTRY

By

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Commonwealth Executive Masters in Business Administration (CEMBA)

DECLARATION

I hereby declare that this submission is my own work towards the Commonwealth Executive Master of Business Administration (CEMBA) and that, to the best of my knowledge, it contains no material previously published by another person nor material which has been accepted for the award of any other degree of the University, except where due acknowledgement has been made in the text.

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Name of Head of Department	**Signature**	**Date**

DEDICATION

This work is dedicated to my husband, Lawrence and son Fausta for your patience, encouragement and emotional support.

ACKNOWLEDGEMENT

I thank the Almighty God, who gave me the strength, protection, continuous guidance and direction in pursuing this programme. My gratitude also goes to my supervisor Dr. Bernard Tetteh-Dumanya for his time, counsel and incredible contribution to the success of this work, to Mrs. Janet Thompson and Mrs. Barbara Banson of CAL Bank for their support and input at the last stage of this study. I also appreciate the support and encouragement from my Mum, siblings and the entire family members

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ABSTRACT

The Banking industry today is characterized by intense competition coupled with rapid changes in customer expectations, increasing regulatory requirements, technological innovation and mounting competition. Failures in processing activities as a result of human errors, fraud and system failures brings significant losses to banks and these losses are key sources of operational risk. Stringent corporate governance, regulatory standards and investor expectations are increasingly making operational risk management a focus for the banking industry. In view of the rising competition within the industry in respect of customer satisfaction and retention, corporate reputation and reward maximization, there is the need for banks to critically align business objectives with risk and control information to enhance operational performance, reduce cost in order to achieve the competitive advantage.

The study focuses on operational risk management and competitive advantage in the Ghanaian banking industry with an objective of identifying the relevance of operational risk management practices in the industry and whether it can be a source of competitive advantage. Closed-ended questionnaires were administered to two hundred and fifty (250) respondents from seven selected banks.

The findings of the study indicated that even though operational risk is quite new in the Ghanaian Banking industry, its effects are being realized. It also reveals that Ghanaian banks are realizing the significance and importance of operational risk management as a tool for gaining competitive advantage and are allocating the requisite resources for it. Some recommendations were made and prominent amongst them were that Banks must link their operational risk management activities to their business objectives and identify the potential

hurdles that hinder their competiveness. Operational risk management is the responsibility of all staff including the Board of Directors and management and as such awareness must be created on the need to identify, evaluate, monitor, control and report operational risk issues in accordance with the strategies and policies of banks in ensuring the adequacy of capital against operational risk.

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LIST OF ABBREVIATIONS

ABL	Access Bank Limited
BBA	British Bankers Association
BBGL	Barclays Bank Ghana Limited
BIS	Bank for International Settlements
BOG	Bank of Ghana
CAL	CAL Bank Limited
CEO	Chief Executive Officer
CIMG	Chartered Institute of Marketing Ghana
DRC	Democratic Republic of Congo
EGH	Ecobank Ghana Limited
GAB	Ghana Association of Bankers
GCB	Ghana Commercial Bank
GSE	Ghana Stock Exchange
ICB	International Commercial Bank
IPO	Initial Public Offer
NSE	Nigeria Stock Exchange
OR	Operational Risk
ORM	Operational Risk Management
RIM	Risk Identification Matrix
UBS	Union Bank of Switzerland
ZBL	Zenith Bank Ghana Limited

CHAPTER ONE

INTRODUCTION

"Operational risk is a daily and continuous 24 X 7 X 365 process. A way of life. Not an event or a meeting at the end of the quarter. Each person and stakeholder at your organization or institution is responsible for it and should live each day embracing it[1].

1.0 Background of the Study

The Ghanaian banking industry is one of the service industries that are significantly contributing to the growth of the economy. It plays a vital role in capital mobilization and also grants financial facilities to businesses that seek to grow and develop. The Banking sector has undergone significant transformation and continues to improve with new regulations and guidelines seeking to maintain stability. This has made the sector more efficient, innovative, competitive and profitable. The transformation of the industry has resulted in an emergence of technologically innovative products and services. Banks have employed these innovative products and services in their operations so as to provide customers with easy accessibility.

In the last five years, the Ghanaian banking industry has seen a phenomenal growth arising from:

a. Capital injection by existing banks to meet minimum regulatory capital requirements,

b. Entry of six banks from the sub region and Asia, and

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[1] Operationalrisk.blogspot.com

c. Expansion in branch network - with bank branches increasing by 53% from 380 in 2005 to 726 in 2010 with 20 new branches springing up in the year 2010 indicating an increase of 3.6%. (Ghana Banking Survey 2010, Bank of Ghana Financial Stability Report – Feb. 2010).

The new capital requirements may lead to an improved buffer for risk absorption in the sector. However, increased competition, growing customer demands, and new regulations are likely to continue to add complexity to business models of banks and information technology environment. These complexities may not be easily unraveled and can lead to the inability to capture or respond rapidly and successfully to emerging external opportunities (Ghana Banking Survey 2010).

On 26 June, 2006, at the official opening of Guaranty Trust Bank the former Governor of Bank of Ghana, Dr. Paul Acquah mentioned in his speech that healthy competition amongst banks has resulted in the continuous growth of assets, liabilities, and incomes in the banking sector. Inspite of this growth, the industry is plaqued with operational risk issues relating to human errors, fraudulent activities and failure in bank systems and processes..

It is in this light that the Bank of Ghana has issued a regulation to all banks to be fully compliant with the Basel II directive of setting aside a portion of their capital to address operational risk issues that may occur. A deadline has been set for 2012 for compliance.

1.1 Problem Statement

Banks today operate in an environment marked by growing consolidation, rising customer expectations, increasing regulatory requirements, technological innovation and mounting competition. In Ghana, the intense competition within the banking industry has generated a greater concern to manage the operational activities of banks in order to avert any possible risks that may occur.

Operational risk is thus seen as a major challenge today and is described as "life threatening" in the banking industry. Operational risk losses have often led to the down fall of many financial institutions. The regulators of financial companies and directors of banks are demanding a far greater level of insight and awareness on the risks they manage, and the effectiveness of the controls they have in place to reduce or mitigate these risks. Further, compliance regulations, like Basel II mandates a focus on operational risks, forcing financial organizations to identify, measure, evaluate, control and manage this ubiquitous risk. This has led to an increased emphasis on the importance of having a sound Operational Risk Management practice in place. This makes ORM one of the most complex and fastest growing risk disciplines in banks and financial institutions.

According to the Governor of the Bank of Ghana, banks in Ghana emerged from the global crisis substantially unscathed partially because of lower global integration, but also due to the strong reliance on domestic deposits to fund banking activities and a regulatory and supervisory framework that limits risky behaviour. Nonetheless, the effect of challenges in the domestic macroeconomic environment since 2008 has given rise to non-performing loans and impaired assets, weakening the balance sheets of some banks.

Looking at what transpired in the global financial system, there is no doubt that the banking industry is crucial to the economy; hence instability within the industry would have negative consequences on the Ghanaian economy. This serves as the basis for safeguarding the sector to ensure equitable, fair and strong business practices and not giving room for complacency. Poor performance or non-compliance with regulations by individual banks can introduce systemic risks and jeopardize the entire banking industry.

There is a growing acknowledgement from banks that a consistent and effective operational risk management framework can help them achieve organizational objectives and superior performance as well as be competitive on the Ghanaian market. Therefore, instead of only aiming to fulfilling regulatory requirements, there is the need to look at operational risk management from another angle - competitive advantage. It was in the light of the above that this study aimed at assessing operational risk management practices in the Ghanaian Banking Industry and how banks could gain competitive advantage through it.

1.2 Objectives of the Study

The study will focus on operational risk management in the banking industry. The objective of the study will be:

General:
- To identify how relevant operational risk management practices are to the banking industry and whether operational risk management can be a source of competitive advantage within the industry.

Specific:
- To appraise how effective operational risk management is being implemented by the banks.
- To assess how operational risk management can be a source of competitive advantage to financial institutions.

1. 3 Hypothesis

The assumption is that:

- Operational risk has an impact on the Ghanaian Banking Industry.
- With a good operational risk management framework in place Banks will be able to gain an advantage over their competitors.

1.4 Significance of the Study

The significance of the study was to reveal the extent to which operational risk affects the activities of banks in Ghana, the need for banks to effectively manage their operational risk to minimize its effect on their operations and how banks could gain competitive advantage through the management of their operational risk. The results will serve as a guide for the banking industry and the business community on how underdeveloped their current operational risk management practices are and the course of action to take in order to effectively utilize their operational risk management policies and strategies to gain competitive advantage. Finally, the study will provide a guide for further studies on operational risk management in other financial institutions.

1.5 Scope of the Study

This study will be centered on Commercial Banks operating in Ghana for the period of 2005 to 2010.

1.6 Limitations

The confidential nature of information on operational risks and bank's code of secrecy made it difficult for employees to willingly provide the needed information. To overcome this constraint the researcher had to promise strict confidentiality of the information that would be provided. The questionnaires were completed under strict anonymity. Another challenge was the difficulty in quantifying operational risk within a short period.

1.7 Organization of the Study

This section describes the content of chapters and sections. ***Chapter one*** provides an overview of operational risk management in general and particularly operational risk management in the Ghanaian banking industry. ***Chapter two*** gives a detailed review of the literature relating to operational risk and operational risk management in the banking industry. ***Chapter three*** looks at the methodological framework of the study. The chapter discusses the types and sources of data, sampling techniques, size and procedures for collection and analysis of data. It also gives a profile of the seven selected bank that will be used to represent the Ghanaian Banking Industry. ***Chapter***

four is the analysis of data and discussions of the findings from the analysis. ***Chapter five*** represents the summary of findings of the study and draws conclusion. It answers specific objectives of the research and makes recommendations based on the findings.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

The objectives of this chapter are to review the existing literature and provide an overview of operational risk in general and in banking industry in particular. The chapter also seeks to show what other researchers have explored in relation to operational risk management and how it can be a source of competitive advantage.

2.1. Definition of key concepts

2.1.1 Risk

Organizations today operate in a dynamic and risky environment and as such they are vulnerable to all kinds of risks in the marketplace, thus making risk an important component of a company's investment strategy. Oxelheim and Wihlborg (1997) define risk as a measure of the timing and magnitude of unanticipated changes, which is evaluated relative to expected changes in variables. These anticipated changes are measured by the expected change, which is normally a result of forecasting.

Tchankova (2002) stated that risk is an inherent part of business and public life. Dynamic market relations continuously increase the uncertainty of the environment where business and public organizations work. There are various types of risks suggested by different authors (Fatemi and Glaum 2000, Croupy, Galai and Mark 2001, and Romero 2003), a summary of which is presented in Table 2.1

Table 2.1: *Types of Risks in Banks*

Credit Risk	Risk arising from inability or unwillingness of a counterparty to honour its credit obligation in accordance with agreed terms.
Market Risk	Result of adverse changes in interest rates, foreign currency exchange rates, equity prices and other relevant market rates, prices and volatilities.
Liquidity Risk and Funding Risk	Risk to the Bank or one of its business units being unable to fund assets or meet obligations at a reasonable cost or, in case of extreme market disruptions, at any price.
Reputation Risk	Reputation risk occurs when negative publicity regarding a bank's business practices leads to a loss of revenue or litigation. It results in the decline of a bank's market or service image.
Operational Risk	The risk of direct or indirect loss to a bank resulting from inadequate or failed internal process, people and systems or external events.
Commodity risk	The risk of changes in the price of commodities.
Interest Rate Risk	The risk arising from possible interest rate differentials in positions mismatch embedded in the balance sheet of the bank.
Compliance Risk	The risk of legal or regulatory sanctions, financial loss that a bank may suffer as a result of its failure to comply with all applicable laws, regulations, codes of conduct and standards of good practices.

Source: Fung 2006, www.wikipedia.com

2.1.2 Risk Management

Risk management is a very important concept for any business as most financial decisions revolve around the corporate cost of holding risk. This issue is particularly important to banks since risk constitutes their core business processes.

According to Pyle (1997), risk management is the process by which managers satisfy these needs by indentifying key risks, obtaining consistency, understandable, operational risk measures, choosing which risks to reduce, which to increase and by what means, and establishing procedures to monitor resulting risk positions.

According to Carey (2001), effective risk management is an efficient and cost effective management technique, which can reduce incidents, claims, wastages and losses. It can also enhance innovation by enabling considered risk taking.

2.1.3 **Operational Risk**

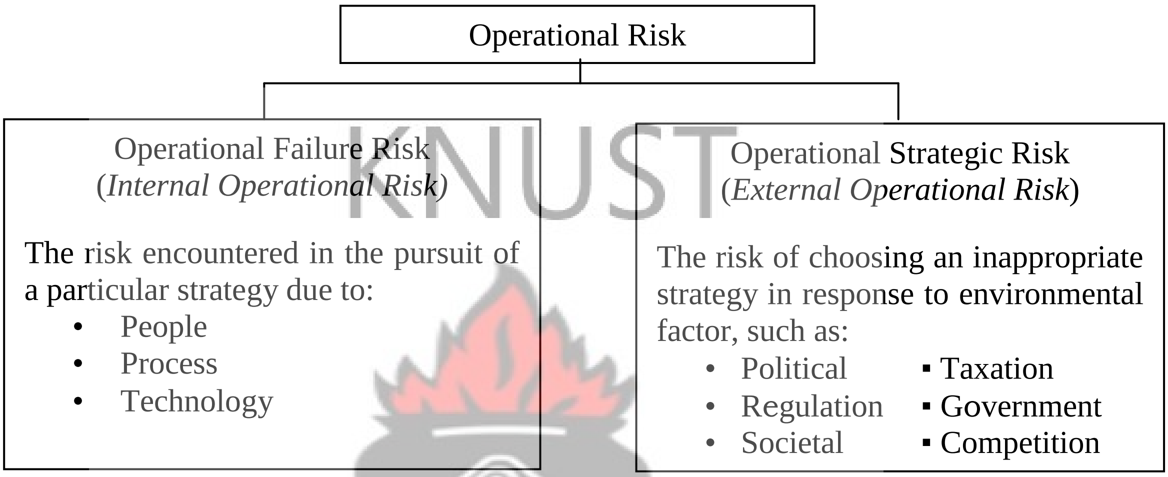
The prerequisite for the theoretical analysis of a problem is the definition of operational risks (Lopez 2002). Mainelli (2002) stated that defining operational risk is complex and even slippery. The term operational risk has only been defined in the last few years. Unlike the definitions of market risk and credit risk which are relatively clear, the definition of operational risk continues to evolve. The Basel Committee on Banking Supervision defines operational risk in the New Basel Capital Accord (2003, p.5) as follows:

> *"Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk, but excludes strategic and reputation risk."*

According to the British Bankers´ Association (BBA) "Operational risk is the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events." Croupy, Galai and Mark (2001), Lopez (2002) and Schroeck (2002) adopted a similar approach to define operational risk, which was risk that could arise both internally and externally. Risk from external events basically covers a lot of different uncontrollable factors, such as natural disaster, terrorism attack that might cause damage to the bank's properties and cause business losses. Lopez

(2002) claimed that internal processes would be closely tied to a firm's specific products and business lines; they should be more specific than the risks due to external events. Two broad of operational risk are categorized in Figure 2.1 below.

Figure 2.1: *Two broad categories of Operational Risk*



Source: Croupy, Galai and Mark 2001, p480

Implication of operational risk events have been experience by the devastating loss of reputation of Arthur Anderson caused by the Enron scandal, the failure of Barings Bank as a result of rogue trading operations or UBS' loss of US$100m due to trader's error (Muermann and Oktem 2002). Hoffman (2002) and the Journal of Compliance Risk and Opportunity (2009) provided a list of the major operational events from 1993 to 2008 (Table 2.2), which indicates that the majority of these losses have occurred in the financial industry.

Table 2.2 *Top Operational Risk Events*

Organization	Loss Amount	Date	Description
Daiwa Bank	US$ 1.1 billion	1993-1995	Loss due to unauthorized trading by an employee.
Barings	US$1 billion	1995	Losses due to lack of dual control and checks and balances.
Sumitomo Corporation	US$2.9 billion	1996	Huge losses incurred through excessive trading of copper.
Numerous Financial Institutions	US$ 20 million (initial estimates)	2001	Terrorists hijacked four commercial airliners and crashed them into the World Trade Center resulting in loss of lives which impacted many businesses.
Citigroup	US$70 million	2004	Failure to comply with federal lending regulations
Bernard Madoff Investment Services LLC	50,000,000,000	2008	Securities Fraud
Societé Generalé Group	7,762,247,360	2008	Unauthorised Trading – Proprietary accounts
Credit Suisse Group	2,660,700,000	2008	Pricing misdeeds

2.2 Operational Risk Management in Banking Industry

Operational risk management in banks has been increasingly emphasized in the past decade. Big financial scandals, frauds and information technology system failures are important drivers for the greater attention both inside and outside banking institutions to their exposures to and internal handling of such risk. The exposure to different kinds of operational risk is nothing new for the individual bank, but as Moosa (2007:167) stresses; “The trend towards greater dependence on technology, more intensive competition, and globalization have left the corporate world more exposed to operational risk than ever before.” For banks, the occurrence of an extreme and major “one-off event in its daily operations may even be more damaging than its credit losses in connection to the current collapse of the financial markets. However, the ability of the bank to properly assess and control, or hedge itself against, the negative economic consequences of such events seems to be less developed than its management of credit and market risks (Flores, Bónson-Ponte & Escobar-Rodríguez 2006; Moosa 2007; Bonsón, Escobar & Flores 2008; Wahlström 2009).

It is important to indicate that the objective of this sub-section is to consider the current operational risk management practice and related issues in the banking industry and not to any recommendation on which best practices to adopt on managing operational risk within the banking industry.

2.2.1 **Approaches in Risk Management**

Calomiris and Herring (2002) stated that firms in general, respond to risks in three different ways: "lay off' the risk, try to reduce the risk; and retain the risk and deal with it by actively managing it. The exact approach a bank adopts for dealing with its risks depends on both the nature of risk and the strategy of the individual organization. This view is also supported by Lopez (2002), when he stated that there was so far no clearly established single way or approach to manage operational risk and that each bank would establish and develop its own method.

Geiger (1999), Bloom and Galloway (2000), Jameson (2001 and 2002) and Allen and Saunders (2002) all agreed that many banks currently adopt a top-down approach, i.e. using a percentage of their non-interest expenses to calculate their operational risk capital. Fung (2006) indicated that there are a number of drawbacks of this approach. This approach does not truly reflect a bank's risk profile against which the capital is required. It is only a rough estimate of the amount of insurance the bank should be carrying to mitigate the effects of potential exposure to operational risk.

It is clear that this top-down approach could no longer meet the real business needs of banks, which increasingly require a more sophisticated means of assessing and mitigating operational risk. For this reason, some of the banks are switching to a bottom-up approach, which can provide a better approach to risk management. A bottom-up approach evaluates operational risk from the perspective of individual business unit that make up an organization’s production process. The advantage of this approach is that it creates a loop so that banks can avoid the worst repercussions of operational failures, such as crisis management and management shake-ups.

2.2.2 Identification in Risk Management

The first step of managing operational risk is to identify it. According to Muermann and Oktem (2002), identifying operational risk is especially challenging in banking industry because the operational factors are not well defined. Geiger (2000) suggested using a risk identification matrix (RIM) to identify and segregate operational risk. The causes are used to differentiate the operational from other risks. Operational risks are all unexpected losses, which have their origin in internal errors, or staff related deficiencies in the processes and systems and also in external events.

2.2.3 Measuring in Risk Management

When the term operational risk management first came on the scene, there were two distinct schools of thought. One school held the idea that it was not possible to manage something which one could not measure and therefore, they stressed on quantitative tools such as loss distributions, risk indicators and economic models. The other school believed that operational risk could not be quantified effectively and therefore they focused more on humanistic, qualitative approaches, such as self-assessments, risk maps and audit findings. However, very soon, people realized the problems of using only one approach but without the others (Geiger 1999, Muermann and Oktem 2002 and Lam 2003). The scope of operational risk is measured by the probability and impact of the unexpected losses from a lack of internal control to external event occurrences.

2.2.4 Managing Operational Risk

Each bank should define their own approach, the extent of the analysis, and which method, either quantitative or qualitative, will be used in the analysis (Davies and Haubenstock 2002). Croupy, Galai and Mark (2001) stated that it was important for a bank to set a clear guiding principle for the operational risk management process which should ensure that it provided an appropriate measure of operational risk across all lines of business throughout the bank. The process of implementing a sound operational risk management should contain certain stage of development.

Davies and Haubenstock (2002) mentioned that good operational risk management needed the support and involvement of senior management who could decide that operational risk was important and deserved attention and the most important point was to allocate resources accordingly. Without their support, operational risk management will be ranked on the last on the list or will be only carry out with the minimum requirement of regulatory body. One important point is that the senior management should play an important role in establishing a corporate environment in which operational risk management can flourish (Croupy, Gala and Mark 2001).

There are various ways of measuring operational risk across the industry. In some of the banks, the responsibility for managing operational risk is with internal audit. However, some of the banks have taken the step of establishing an independent corporate function (Mainelli 2002). Croupy, Gala and Mark (2001) stressed that operational risk should be managed as a partnership of business units, business infrastructure groups, and corporate governance units such as internal audit and risk management.

Regarding allocating capital to operational risk, there is an uncertainty among the banks about which Accord approach is most appropriate. In the Deloitte and Touché (2001) survey, the majority of the participants indicated that their existing operational risk processes would not be able to facilitate compliance to the Basel Accord. However, Bloom and Galloway (1999 and 2000), Davies and Haubenstock (2002), Massoud and Raibom (2003) and Denayer (2004) all agreed that the development of operational risk management was more than a regulatory compliance issue. Early adopters of more sophisticated operational risk management have reported significant business benefits, including improved customer service, greater operating efficiency and reduced losses. To fully realize these benefits, it is clear that further development of operational risk management practices must integrate quantitative and qualitative tools.

2.3 Bank regulation on Operational Risk

Traditionally, banks have focused largely on credit risk management and market risk management, with only limited resources being allocated to operational risk management. The fact that operational losses have increased markedly over recent years has prompted regulators and banks to take a closer look at operational risk management. The Basel Committee has been working to set standards for both how operational risk is measured and the capital which regulators require banks to hold for the operational risk they take.

The supervisory authorities have only recently started to take a closer look at operational risks. In September 1998 the Basel Committee published an initial report on this topic, without mentioning the question of regulation. The report merely said: "The Committee will continue to monitor developments in this area."

According to Mainelli (2002) and Lewis (2004) regulators are beginning to take a tough view on operational risk and severe financial penalties for failing to monitor and control operational risk are now a reality.

2.3.1 Risk Financing and Operational Risk Management

Banks have various options to dealing with operational risk. They can avoid the risk, retain the risk by developing controls to reduce the frequency and severity of the losses or they can choose to absorb these losses through its earnings. Other financing options available to them are:

2.3.1.1. Insurance

Insurance in recent times has been seen as a valuable instrument through which banks can transfer their operational risk activities. Its forces banks to analyze thier Operational Risk and to differentiate between its impact and frequency. Insurance companies offer banks specialized products that protect them against direct financial loss (loss of money as well as assets) caused by any act of fraud on the part of any employee. Directors' and officers' liability coverage can protect against losses incurred by directors and officers for alleged wrongful acts and by the firm for money it paid to directors and officers to indemnify them for damages. Property insurance can protect firms against losses from fire, theft, inclement weather, etc.

2.3.1.2 Outsourcing

Outsourcing business processes to specialized service providers is fast emerging as a tool for operational risk transfer and a common practice in the Banking industry today. Enormous competition and rapidly dwindling bottom lines have compelled banks to renew their focus on their cost strategy by outsourcing certain aspects of their business activities including information technology (e.g., applications development, programming etc), specific operations (e.g., some aspects of finance and accounting, back-office activities and processing etc), and contract functions (e.g., direct sales, front office activities etc). For effective risk transfer, the relationship with the outsourcing partner should be managed effectively through Service Level Agreements, which should clearly determine the rights, responsibilities and expectations of both the parties.

2.3.2 Basel Accord, Basel II and Basel III Accords

The Basel Committee proposed a set of minimal capital requirements for banks which became law in G-10 countries in 1992 (BIS, 2004). The requirements came to be known as the 1988 Basel Accord, which primarily addressed banking in the sense of deposit taking and lending and its focus was on credit risk. Banks were subject to an 8% capital requirement. Specifically, they would calculate metrics for capital and credit risk and with a requirement that the factor of capital and credit risk must be larger of equal to 8%. In January 1999, the Basel Committee proposed a new capital accord, which has come to be known as Basel II. It then followed with an extensive consultative period, with the committee releasing additional proposals for consultation in January 2001 and April 2003. The finalized Basel II Accord was released in June 2004 and based on three pillars: minimum capital requirements; supervisory review; and market discipline.

“Basel III" is a comprehensive set of reform measures, developed by the Basel Committee on Banking Supervision, to strengthen the regulation, supervision and risk management of the banking sector. These measures aim to:

- Improve the banking sector’s ability to absorb shocks arising from financial and economic stress, whatever the source
- Improve risk management governance
- Strengthen banks’ transparency and disclosures.

These consultative documents formed the basis of the Committee's response to the financial crisis and are part of the global initiatives to strengthen the financial regulatory system that have been endorsed by the G20 Leaders. Basel III is part of the Committee's continuous effort to enhance the banking regulatory framework. It builds on the International Convergence of Capital Measurement and Capital Standards document (Basel II).

2.4 Key Success Factors and Competitive Advantage in the Banking Industry

The critical success approach is one of the accepted methods that are based on the technique of factor analysis for corporate strategic planning, which aims to identify factor structures present in a set of variables (Chen, 1999). According to Sureshchandar et al (2002), factor analysis identifies relatively small number of factors that represent relationships among a set of interrelated variables.

Critical success factors have been defined in several ways depending on the purpose for which they were used (Fung 2006). For the purpose of this paper, Rockart’s (1979) definition will be used. He defines critical success factors as "the limited number of areas in which results, if they are satisfactory, will ensure successful competitive performance for the organization". Critical success factors are those factors that must go right for the organization to achieve its mission. They provide management with a measure on which improvement efforts can be focused (Martin and Palakshappa 2003).

Bamberger (1989) stated that critical success factors and the firm's competitive ability are the two main components of the competitive advantage of a firm. With regard to the banking industry, Johnson and Johnson (1985) proposed that the width and depth of the product and service line, low operating costs, and a good bank reputation can be considered as the three critical success factors in a competitive market. Canals (1993) recognized that the concepts of value chain and bank configuration could be employed to develop a bank's competitive advantage. He identified four sources of a bank's competitive advantage, namely manpower, financial management, asset base and intangible assets. In 1993, Wilde and Singer identified only three critical success factors for banks, namely low costs, product differentiation and financial strength.

Chen (1999) derived four critical success factors in the banking industry, which could reflect four business goals for the commercial bank manager. They were the ability of bank operation management, bank marketing, developing bank trademarks and financial market management. According to Chen (1999), the ability of bank operational management was one of the most important critical success factors.

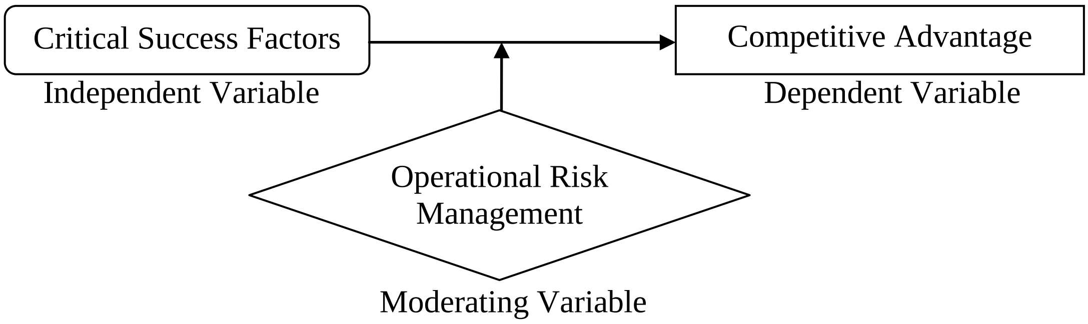
Reputation has been proven as both entry barrier and competitive advantage in financial services industry (Fung 2006). Reputation refers to quality and independent advice, integrity and broad range of products, relation orientation and services. By using reputation as a "tool", banks can both gain business from its competitors and attract best people in the industry to work for it. The other source of competitive advantage in banking industry includes also people and strength of network (Turnbull and Moustakatos, 1996). Denayer (2004) stated that operational risk management was seen as improving process effectiveness and managing external risks such as reputation and regulatory risks. In other words, operational risk management can provide competitive advantage rather than just avoiding negative outcomes.

Operational risk management is nowadays seen as improving process effectiveness, sponsoring better communication and managing external risks such as reputation and regulatory risk. This means providing competitive advantage and not just avoiding negative outcomes (Denayer 2004). Young and Theodore (2003) identified that a sound operational risk management would also affect credit rating, share prices and organizational reputation. Investors and analysts are increasingly paying more attention in their assessment of management, their strategy and the expected long-term performance business. Bloom and Galloway (1999) stated that proactive operation could protect a firm from potential damage and could result in the protection of shareholder value, avoidance of regulatory censure or burden, the ability to render services without interruption, and the maintenance of a good reputation and public and investor confidence in the long run. Ultimately, the benefit of proactive operational risk management will lead to greater efficiencies and lower costs for lending money, hence enabling a firm to achieve competitive advantage (Fung, 2006).

2.5 Conceptual Framework

The conceptual framework developed for this research (Figure 2.2) is based on the assumption that there are various risks surrounding the banking industry among which Operational risk is the most relevant.

Figure 2.2: *Conceptual Framework*



The independent variables in this conceptual framework are the critical success factors in banking industry, which have been discussed in Chapter 2. There are various critical success factors within a bank which will lead to the bank achieving competitive advantage against its rival. So far, there is no universal agreement as to which are the most important critical success factors in banking industry. For this research, it is hypothesized that the following are the six main critical success factors which were perceived as sources of competitive advantage in banking industry. They are Staff, Strength of Network, Primary position in domestic business, Image and reputation, Product Differentiation, Technology. The results of the study on the Ghanaian banking industry which will be discussed in Chapter 4 will reveal whether the above factors are critical in the banking industry.

The dependent variable in this study is competitive advantage. Devlin and Ennew (1997) suggested that competitive advantage must be built around attributes that customer value and product which consumers perceive as substitutes for each other. In this study, it was perceived that staff, strength of network, primary position in domestic business, image and reputation and product differentiation were the most important critical success factors (independent variable) in banking industry, and they would help a bank to gain competitive advantage (dependent variable).

CHAPTER THREE

METHODOLOGY AND ORGANIZATIONAL PROFILE

3.0 Introduction

The aim of every research work is to design research tools and techniques that effectively capture, validate and measure the key characteristics in order to arrive at the desired goals of the research. This chapter discusses how the fieldwork was organized and the techniques adopted to collect the relevant data for the study as well as the data analysis techniques used.

3.1 Sources of Data

The research called for gathering of both secondary and primary data.

3.1.1 Primary Data

The primary data was sourced from questionnaires, which were administered to 250 staff of the seven (7) selected Banks (Ecobank, CAL Bank, Ghana Commercial Bank, Zenith Bank, Access Bank, International Commercial Bank and Barclays Bank), the Bank of Ghana and the Ghana Association of Bankers.

3.1.2 Secondary Data

The secondary data was sought from Annual Reports of Banks, banks' documentation on Operational Risk as well as other existing relevant literature.

3.2 Population

In order to ascertain adequate information on the Ghanaian banking industry and have a fair representation of the industry the following banks were selected in the following category:

a. Zenith to represent the Nigerian Banks

b. ICB to represent the Asian Banks

c. Barclays Bank to represent the European Bank

d. Ghana Commercial Bank to represent the local banks

e. Ecobank which is a Pan-African Bank

f. Access Bank which is the latest Bank in the industry. It is hoped that they might have new way of dealing with operational risk.

g. CAL Bank

A sample size of 250 was be used and this was drawn from the seven banks Zenith Bank – 30, Ghana Commercial Bank – 60, Barclays Bank - 50, Access Bank – 15, Ecobank – 40, CAL Bank 30, Bank of Ghana – 20, Ghana Association of Bankers 5). The response rate was 80% which is very encouraging.

3.3 Sampling Technique

The researcher used the purposive and simple random sampling techniques to select the sample. The reason behind the choice of this technique was to ensure that each member of the population had equal chance of being selected for the study and that those who mattered in the study were strictly involved. Quantitative approach was used in order to prevent elements of bias in the gathering and presentation of data. It also ensured objectivity, and reliability of the research undertaken.

3.4 Data Collection Instruments

3.4.1 Questionnaire

A questionnaire is a list of carefully structured questions with a view to exploring a reliable response from a chosen sample (Hussey and Hussey 1997). Close-ended questions were used for the questionnaire. The questionnaire and an information sheet explaining the purpose of the study were distributed to management and staff of the seven banks selected to represent the Banking Industry in Ghana. In order to maximize the chances of obtaining adequate responses, the length of the questionnaire was taken into consideration and the terms used in the questionnaire was not technical, therefore, no explanations were needed.

Table 3.1: *Overview of Questionnaire*

Questionnaire Section	No. of Questions	Purposes
Risk in the banking industry	3	Reveal the perceived important and relevant of various risk in Ghanaian banking industry
Objectives/Strategies on operational risk management	6	Gain in-depth knowledge the current operational risk management practice in banking industry in Ghana
Perceived critical success factors in the Banking Industry which leads to competitive advantage	13	Reveal the perceived critical success factors in Ghanaian banking industry and whether these factors can lead to competitive advantage.

Source: Field Data

The majority of the questions from section one were sourced from a previous study (with slight modifications), which was carried out by Fung (2006) with Licensed Banks in Hong Kong.

Respondents were first asked to rank the relevance of each of the main risks type, which included liquidity, reputational, environment, operational, market, credit, legal and any other risk category which they perceived relevant to banking industry as well as the indicate the relevance of each of them to their bank in which they worked.

In the second section, respondents were asked to indicate the objective and strategies of operational risk of the banks for which they work. It is important to emphasize that the purpose of this session is not intended to ascertain the kind of best practice on operational risk management in the Ghanaian Banking industry. Rather, it is hoped that through this section, responses would provide a general overview of the current operational management practice in industry.

In section three, respondents were asked to indicate the perceived critical success factors in the banking industry, which could contribute to competitive advantage. The critical success factors were based on the literature. Six independent variables were measured:

a. Staff (Canals 1993, Turnbull and Moustakatos 1996)
b. Strength of network (Turnbull and Moustakatos 1996)
c. Primary position in domestic business (Turnbull and Moustakatos 1996)
d. Image and reputation (Johnson and Johnson 1985; Tumbull and Moustakatos 1996; Devlin and Ennew 1997)
e. Product differentiation (Johnson and Johnson 1985; Wilde and Singer,1993; Canals 1993)
f. Technology
g. Operational risk management

To ensure validity of the instruments, the questionnaire was pretested before it was re-administered. The purpose was to ensure that anomalies were corrected so that the items could measure exactly what it was intended to measure.

3.5 Data Analysis Technique

Following the gathering of completed questionnaires, total responses for each question were tabulated and developed into tables and graphical diagrams. These were used to analyze risk in the selected banks, objectives/strategies on operational risk management adopted by the banks and the perceived critical success factors in the Banking Industry. With the help of the literature, the variables (operational risk, critical success factor and competitive advantage) were identified and the questionnaire items were designed to cover them. The measurements of the variables have been well explained in the conceptual framework in this chapter.

3.6 Profile of Banks

3.6.1 Ghana Commercial Bank Limited (GCB)

GCB, Ghana's first indigenous bank was established in 1953 to serve the less affluent in society because majority of Ghanaians could not meet the demands and requirement of the foreign banks. The Bank had been wholly government owned until 1996 when under the economic recovery programme part of the government ownership was divested. Today government ownership stands at 21.36% while institutional and individual holdings add up to 78.64%.

From the one branch of the 1950s, GCB now has over 150 branches and 11 agencies throughout the country. The growth of the Bank has been synonymous with its customer base. During the first five years of the Bank's operations, our customers were mainly small Ghanaian traders (now termed SMEs) and other nationals who were expected to maintain credit balance accounts because the Bank was then not adequately capitalized. From the small trader as customer, GCB now has a customer profile that ranges from salaried workers through small and medium scale entrepreneurs to large trading concerns, quasi-governmental institutions and corporate customers. Today we can boast of being the widest networked Bank in Ghana (http://www.gcb.com.gh/page.php?pid=1)

3.6.2 **Ecobank Ghana Limited (EGH)**

Ecobank Ghana limited was chosen for this study because of its reputation as being among the top four banks in Ghana. It is also listed on the Ghana Stock Exchange and therefore has its financial and other regulatory reports published, ensuring that the public has access to some basic information. Over the past decade EGH has won several banking awards in various categories including the coveted ―Bank of the Year Award for five consecutive years. According to the 2010 Banking Survey Report released by PricewaterhouseCoopers Ghana in collaboration with the Ghana Association of Bankers, EGH is ranked the fourth largest bank in terms of total assets contributing 10.1% to total assets of the banking industry. The bank was the third largest contributor to both industry deposits and gross loans and advances with 10.5% and 7.7% respectively. (Asare-Bekoe K. 2010).

3.6.3 **Zenith Bank (Ghana) Limited (ZBL)**

Zenith Bank (Ghana) Limited is a private limited company which commenced universal banking operation in September 2005 with a capital base of GH¢10.8 million. The bank is a subsidiary of Zenith Bank PLC, one of the largest banks in Nigeria by all measures, with"AAA" ratings, and the Euromoney Best Bank in Africa for 2007. ZBL currently operates twenty-three branches and agencies, connected online, real time and with ATM facilities. It operates with the objective of making banking easier and better than anything customers have ever experienced. Among its most distinguishing traits are its cutting edge ICT platform which sets it apart from competitors, its passionate staff and its devotion to the development of systems and products to satisfy customer specifications. The bank was adjudged the Bank of the Year in Ghana as well as the Best Bank in Financial Performance in the country for the 2008 financial year, in addition to other awards won over the years at the Corporative Initiative, Ghana Banking Awards, 2009.

Zenith Bank was chosen as one of the banks to represent the Ghanaian Banking industry due to the major role in the transformation of the banking industry into an intensely competitive, customer oriented, more efficient and technologically inclined industry (2010 Annual Report of Zenith Bank).

3.6.4 International Commercial Bank (Ghana) Limited (ICB)

International Commercial Bank Ghana Limited was issued with its universal Banking License in Nov, 1996 under the Banking Act, 2004 (act 675). The Bank is owned by ICB Financial Group Holding based in the Switzerland. International Commercial Bank Ghana Limited is the First Branch in Africa and the Fifth of ICB Financial Group Holding.

The Bank operates with seventeen branches in five out of ten regions in Ghana and has a started capital of GH¢ 60 million. With a team of high calibre staff with diverse skills and experience, the Bank offers a comprehensive range of products and services to meet the banking and financial need of existing and potential customers.

Recognizing the opportunities in the Ghanaian Financial Service industry, International Commercial Bank's mission is to achieve excellence in all areas of banking and financial business that we serve.

3.6.5 **Barclays Bank Ghana Limited (BBGL)**

Barclays has operated in Ghana for ninety four years. It is a wholly owned subsidiary of Barclays Bank PLC. Its vision is to become the best bank for every customer, in every branch, for every product and every time. BBGL has an expansive retail and commercial banking network in the country with 92 branches and over 130 ATMs in all regional capitals and major towns. Its products and services are targeted particularly at the business and corporate, as well as retail customers. Barclays offers a wide range of commercial, Retail and Treasury products and services. It also offers local business banking product and services for Small Medium Enterprises and indigenous businesses.

The Bank of Ghana in February, 2010 named Barclays Bank of Ghana Limited the biggest foreign bank and also the largest bank in terms of capacity to handle transactions in Ghana. The Bank's Premier Banking offers tailor made solutions and one-on-one banking to its high net worth. The bank's sustainability programme focuses on three pillars. Banking for brighter futures; Looking after local communities and

Charity begins at work. Barclays uses these key pillars to support developmental projects across Ghana (http://www.barclays.com/africa/ghana/barclays_in.htm)

3.6.6 Access Bank Limited (ABL)

Access Bank (Ghana) Limited is the latest entrant into the Ghanaian financial industry at end of 2010. The Bank is currently one of the most capitalized banks in the country, having received its universal license from the Bank of Ghana in May 2009. The bank commenced operations with a stated capital base of GH¢80 million, well in excess of Bank of Ghana's stipulated minimum capital requirement of GH¢60 million for universal banks. Access Bank Ghana is owned by Access Bank Plc, a full-fledged financial services provider operating through a network of over 120 branches in Nigeria.

In Ghana, the bank is committed to delivering a new experience in world-class banking through leveraging the enterprise-wide competencies within the Group. As part of this, the bank provides tailored solutions to meet the needs of corporate and commercial clients. The Bank aims to transform the local banking landscape and to serve as the reference point for global best practices in the Ghanaian financial industry (www.accessbankplc.com/gh).

3.6.7 CAL Bank Limited (CAL)

CAL Bank commenced operations in July 1990 and acquired a Universal Banking license in 2004. Upon acquiring the universal banking license, the Bank expanded its retail banking operations along an array of impressive specialized products and services.

In 2004 CAL was listed on the Ghana Stock Exchange (GSE) with a successful IPO of US$7m which was oversubscribed by 350%. Six years on, the bank issued a rights issue which was taken up by about 50.62% of its existing shareholders. The Bank's Slogan "Bank on our Service" is testament to the bank's ethos of customer delight. This has been the underpinning philosophy driving the bank into being continuously acknowledged in Ghana as the most customer-centric and innovative financial institution. CAL Bank plays an important role in the Ghanaian financial sector by providing total banking services to personal, commercial and corporate clients in Ghana. In 2008 the Bank was adjudged the best Bank of the year by the Chartered Institute of Marketing. Other awards have also been won by the Bank from 2007 to 2009. (www.calbank.net)

Table 3.2: *Important Statistics on seven banks selected to represent the Banking Industry in Ghana*

Characteristics	**BBG**	**GCB**	**ICB**	**Zenith**	**EBG**	**ACCESS**	**CAL**
Year of incorporation	1917	1953	1996	2005	1990	2008	1990
Asset Size	1,324,394	1,819,507	166,237	535,130	1,275,266	84,749	430,154
Number of Branches	83	157	12	16	48	2	14
Asset Ranking	2	1	21	8	4	23	12
Current Banking License	Universal	Universal	Universal	Universal	Universal	Universal	Universal
Ownership	Foreign	Local	Foreign	Foreign	Foreign	Foreign	Local
Market Share %	10.8%	14.3%	1.4%	4.1%	10.1%	0.7%	3.4%

Source: Ghana Banking Survey 2010, Bank's websites and annual reports

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

4.0 Introduction

The main objective of this chapter is to discuss and analyze the findings arising out of the data collected.

4.1 Gender of Respondents

***Table 4.1**: Gender of Respondents*

Gender	Frequency	Percentage
Male	155	78%
Female	45	23%
Total	**200**	**100%**

Source: Field Data 2011

Table 4.1 shows that efforts were made to get a good representation of both sexes. Even though male dominated (78%) as compared to (23%) female, the survey method showed that both genders were well represented.

4.2 Analysis of results/responses

A total of 250 questionnaires were distributed to the seven selected banks to measure the relevance of operational risk and whether operational risk can be a contributing factor for Ghanaian banks to gain competitive advantage within the industry. A total of 200 questionnaires were received based on which the following analysis have been made.

4.2.1 Risks in the Ghanaian Banking Industry

The result of the various types of risked as ranked by senior management within the Ghanaian banking industry is outlined from Table 4.2 to 4.4.

***Table 4.2**: Relevance of various types of risks in banking industry*

Type of Risk	Respondents	Percentage
Environmental	10	5%
Market Risk	49	25%
Operational Risk	46	23%
Credit Risk	55	28%
Legal Risk	8	4%
Reputational Risk	13	7%
Liquidity Risk	19	10%
Total	**200**	**100%**

Source: Field Data 2011

28% of the respondents ranked credit risk as the most relevant in the banking industry. Market risk was second with 25% of the respondent ranking it as the most relevant in the industry. Operational risk was ranked by 23% of the respondents as the third most relevant. Liquidity Risk and Reputation Risk was ranked fourth and fifth by 10% and 7% of the respondents respectively, while 5% of the respondents ranked Environmental risk as the sixth with the final 4% indicating that legal risk within the industry was the least relevant.

***Table 4.3**: Frequency of assessment and quantification of the Types of Risks*

Type of Risk	Annually	Semi-Annually	Quarterly	Monthly	Weekly	Daily
Environmental Risk			8%			
Market Risk						13%
Operational Risk					20%	
Credit Risk						23%
Legal Risk				15%		
Reputational Risk		5%				
Liquidity Risk						18%

Source: Field Data 2011

From the Table 4.3, 23% of the respondents indicated that Credit Risk was assessed and quantified weekly whilst operational risk according to 20% of respondents noted it was done on a monthly basis. 18% and 15% of the respondents indicated that liquidity risk and legal risk were assessed and quantified on a weekly and quarterly basis respectively. 13% of the respondents said market risk was assessed and quantified on a daily basis with 8% and the remaining 5% indicated that environmental risk and reputation risk were assessed and quantified on a semi-annually and annual basis.

Table 4.4: *How regular are the following risks formally managed*

Type of Risk	**Annually**	**Semi-Annually**	**Quarterly**	**Monthly**	**Weekly**	**Daily**
Environmental Risk		5%				
Market Risk						25%
Operational Risk				25%		
Credit Risk					30%	
Legal Risk			1%			
Reputational Risk	3%					
Liquidity Risk					12%	

Source: Field Data 2011

Referring to Table 4.4, 30% of the respondents noted that Credit Risk was managed weekly whilst operational risk according to 25% of respondents. 25% of respondents indicated that market risk was managed daily with another 12% saying that liquidity risk was managed weekly. 5% and 3% of the respondents noted that environmental risk and reputational risk were managed on a semi-annually and annually respectively while the final 1% said legal risk was managed on a quarterly basis.

4.2.2 Objective/Strategies on Operational Risk Management in the Ghanaian Banking Industry

The results of how the relevance of different kinds of risk was rated by managers in the banking industry are reported from Table 4.5 to 4.10.

Table 4.5: *Relevance of Operational Risk Management to the Ghanaian Banking Industry*

Options	Respondents	Percentage
Yes	130	65%
No	20	10%
I do not know	50	25%
Total	**200**	**100%**

Source: Field Data 2011

When asked about the relevance of operational risk to the banking industry in Ghana, 65% of the respondents answered "Yes" with another 25% indicating that Operational Risk Management was not relevant. The remaining 10% did not know whether operational risk was relevant in the banking industry or not.

Table 4.6: *Importance of current risk management practices to banks*

Scores	Respondents	Percentage
1	0	0%
2	10	5%
3	15	8%
4	60	30%
5	115	58%
Total	**200**	**100%**

Source: Field Data 2011

In reference to Table 4.6, from the scale of 1 (not important) to 5 (very important), 58% of the respondents ranked the importance of current risk management practices as very important to Ghanaian banks at 5. The remaining 30% ranked it at 4. 8% ranked it at 3with the remaining 5% ranking it at 2. None of the respondents however indicated that the current risk management practices in Ghanaian banks were not at all important.

Table 4.7: *Ability of Banks to allocate resource towards ORM Policy and Practice*

Scores	Respondents	Percentage
1	0	0%
2	0	0%
3	27	14%
4	68	34%
5	105	53%
Total	**200**	**100%**

Source: Field Data 2011

From Table 4.7, 53% of the respondents said their banks significantly allocate resources towards ORM policies and practices. On a scale of 4, 34% said their banks allocated resources for the same course with the final 14% ranking the allocation of resources of their banks towards ORM policies and practices at 3.

Table 4.8: *Linkage between Bank's strategic objectives and management of operational risk*

Scores	Respondents	Percentage
1	0	0%
2	0	0%
3	15	8%
4	50	25%
5	135	68%
Total	**200**	**100%**

Source: Field Data 2011

Asked whether there was a linkage between their bank’s strategic objectives and the management of operational risk (from the scale of 1 to 5) 68% of the respondents said the linkage was significant (Scale 5). Another 25% said it was quite significant (Scale 4) with the remaining 8% ranking the linkage at scale 3.

Table 4.9*: Importance of effective ORM to achievement of Bank's objectives*

Scores	Respondents	Percentage
1	0	0%
2	0	0%
3	0	0%
4	35	18%
5	165	83%
Total	**200**	**100%**

Source: Field Data 2011

From Table 4.9 from a scale of 1 (not at all) to 5 (very important), 83%of the respondent indicated that effective ORM is very important to the achievement of their bank's objectives. The remaining 18% ranked the importance of ORM to the achievement of their bank's objectives at 4.

Table 4.10*: Availability of Internally developed ORM processes or guidelines*

Options	Respondents	Percentage
Yes	125	63%
No	75	38%
Total	**200**	**100%**

Source: Field Data 2011

Asked whether their banks have internally developed ORM processes or guidelines, 63% of the respondent answered in the affirmative with the remaining 38% indicating that their banks had not developed any ORM processes or guidelines internally.

4.2.3 Critical success factors and competitive advantage

The overview of how competitive advantage is perceived in banks and the relationship between the variables: staff, strength of network, position in domestic market, image and reputation, product differentiation, internal guidelines and policy on operational risk management, technology and competitive advantage are indicated from Tables 4.11 to 4.14.

Table 4.11: Extent to which bank's perceive ORM as a source of competitive advantage

Scores	Respondents	Percentage
1	0	0%
2	0	0%
3	15	8%
4	63	32%
5	122	61%
Total	**200**	**100%**

Source: Field Data 2011

From Table 4.11, 61% of the respondent indicated that their bank's perceive ORM as a source of competitive advantage significantly (rank 5). 32% indicated that the way their banks perceived ORM as a source of competitive advantage was quite significant (rank 4). The remaining 8% of the respondents ranked their banks at 3.

Table 4.12: Perception of banks on how OR losses will impact on their competitive advantage

Scores	Respondents	Percentage
1	0	0%
2	0	0%
3	25	13%
4	75	38%
5	100	50%
Total	**200**	**100%**

Source: Field Data 2011

From Table 4.12, 50% of the respondents indicated that their banks perceive that OR losses will impact on their competitive advantage significantly (they ranked their banks at 5 from a scale of 1 to 5). Another 38% of them ranked their bank at. The remaining 13% ranked their bank at 3.

Table 4.13: *Perceived sources of competitive advantage in bank*

Options	Respondents	Percentage
Staff	40	20%
Strength of network	15	8%
Primary position in domestic market	25	13%
Image and Reputation	20	10%
Product Differentation	15	8%
Internal Guideline and Policy on ORM	20	10%
Technology	65	33%
	200	**100%**

Source: Field Data 2011

From Table 4.13 respondents were asked to indicate which of the listed factors is perceived to be a source of competitive advantage for their banks. 28% of them said Staff, 25% of them said technology with another 13% and 10% indicating that primary position in domestic market and image and reputation were sources of competitive advantage respectively. Another 10% of the respondents said bank's internal guidelines and policies on ORM is a source of competitive advantage with 8% opting for product differentiation. The final 8% said bank's strength of network (relationship with other institutions) was a source of competitive advantage.

Table 4.14: *Importance of perceived sources to competitive advantage*

Options	Respondents	Percentage
Staff	47	24%
Strength of network	15	8%
Primary position in domestic market	23	12%
Image and Reputation	25	13%
Product Differentation	15	8%
Internal Guideline and Policy on ORM	30	15%
Technology	45	23%
	200	**100%**

Source: Field Data 2011

Analysis from Table 4.14 is a follow upon on results from Table 4.13. Here respondents were asked to indicate how important the perceived sources were to competitive advantage. 24% of the respondents said Bank staff was important with another 23% and 15% indicating that Technology and internal guidelines and policies on ORM respectively were important. Another 13% and 12% of respondents said image and reputation, and primary position in the local market were important respectively. 8% of them said the product differentiation of banks was important whilst the final 8% said the strength of their bank's network was important.

4.3 Discussions of results/responses

4.3.1 Introduction

From the literature review in Chapter 2 of this study it is evident that the Banking industry is characterized by all kinds of risks with operational risk being the newest of them. From the survey it is clear that these risks (environmental, legal, market, credit, liquidity, reputation and operational) are all inherent in the day to day activities of Ghanaian banking industry. Even though all these risks are critical in the industry market, credit and operational risks are the most relevant looking at the responses from the various respondents. Of the three, operational risk which is ranked third is the newest. This notwithstanding it is important to note that all these seven types of risks are relevant and management of banks must assess and manage them effectively to avert losses that might occur as a result of any of them.

4.3.2 Operational Risk Management and its Implementation

The survey shows that though all these risks are relevant they are not all assessed and quantified frequently. Of the seven, credit, market and operational risks are the ones that are most frequently assessed. This can be attributed to the fact that the day to day activities of banks involves money and people. Banks must therefore pay particular attention to them on a daily basis to ensure they are kept under control. Though operational risk is quite new in the industry, it is being assessed and quantified on a weekly basis. This proves what has been highlighted in the literature review that operational risk is very important and critical to the success of banks.

Assessing and quantifying these risk is not sufficient to safeguard banks from losses. All these risks have to be managed effectively and efficiently if banks are going to operate successfully. The survey indicates that of all the risks, credit and liquidity are managed weekly. This can be explained by the fact that banks' business activities bothers mainly on giving out credits to customers and the ability or inability of customers to honour their commitments affects the liquidity position of banks. Operational risk management is managed on monthly basis. This proves the point made in earlier chapters that the Ghanaian banking industry has not fully embraced the concept of operational risk and its management. Even though all the seven types of risk are relevant to the industry, managing environmental risk on a semi-annual basis can be attributed to the fact that the environment within which banks operate is quite stable.

The survey also indicated that reputation risk and legal risks are managed on an annual and quarterly basis respectively. This can be explained that with the effective and efficient management of all the other risks banks will not have a cause to worry about legal and reputational issues. From the survey and subsequent discussion above, it can be concluded that risk in the banking industry in general and the Ghanaian banking industry in particular. The identification and management of these risks is therefore central to delivering on the corporate objective of banks. By understanding and managing risks banks provide greater certainty and confidence for their shareholders, employees, customers, suppliers, and for the communities within which they operate.

4.3.3 Operational Risk Management and Banks' Strategies

Operational risk as discussed earlier is quite new in the Ghanaian banking industry. Respondents were asked for their views on the objectives and strategies that their individual banks have on operational risk management. Majority (65%) of the respondents expressed the opinion that Operational Risk management practices are important to the Ghanaian banking industry. This can be explained by the regulatory requirement by Bank of Ghana for all banks to ensure compliance of the Basel II directive which is to set aside a percentage of their capital to cater for operational risk issues that might arise out of their day to day business activities.

Whilst some Ghanaian banks are now setting up operational risk units others are ensuring that desks are being created within their risk department to handle operational risk management issues. Due to the serious nature of Operational Risk management, bank executives are gradually embracing it. This is evident in banks allocating resource towards operational risk management policies and practices. This proves the commitment of bank executives including the board to develop and maintain risk control systems. Majority of respondents attest to this.

Majority of the respondents (68%) see their banks' strategic objective to be linked with the managing of operational risk. This can be explained by the fact that operational risk management is increasingly seen as an indicator of underlying corporate quality and sustainable financial performance coupled with growing regulatory pressure on banks to have their operational risks well in hand. Strategies and objectives are developed by board of directors and management of banks. For banks to be seen to be linking their strategies and objectives to managing operational risk proves that senior management of banks are now putting operational risk management on top of their agenda.

From the responses, majority of the respondents (83%) indicated that effective operational risk management can aid in achieving bank objectives. Objective of Ghanaian banks' is not only to make profits by giving credits but also to ensure that they tailor their products and services to meet the requirements and expectations of their customers. Without effective management of operational risk, banks cannot monitor its market and credit exposure.

Majority of respondents are of the opinion that their individual banks have internally developed operational risk management processes or guidelines. This is however not encouraging because operational risk management as discussed is key to achieving bank objective. All banks must therefore ensure to develop operational risk management processes and guidelines. These guidelines must be comprehensive in nature and must cover all areas of operational risk (human resources, internal control systems and processes, reporting guidelines, culture and management information).

4.3.4 Operational Risk Management and Competitive Advantage in Ghanaian Banks

The Ghanaian banking industry has become dynamic and highly competitive. With numerous bank products and services they are in constant completion with each other for customers. This has made banks more customer-focused. When asked their views on the extent to which banks perceive operational risk management as a source of competitive advantage, majority of respondents indicated that operational risk management can be a source of competitive advantage. Effective operational risk management has become a key component of competitive advantage as investors look out for elements of risk management as indicators of underlying corporate quality and sustainable financial performance. Again majority of respondents (50%) perceive that losses associated with operational risk will have an impact on their banks' competitive advantage. As indicated in the literature review, Operational risk losses are as a result of human errors, fraudulent activities, failure of systems, lack of processes or excessive processes and external factors such as disasters through natural causes. The perception of banks affirms earlier facts that operational risk is real in the banking industry and its losses are detrimental to the survival and growth of banks. Management must therefore put in place strategies to ensure that these operational risk factors outlined above are managed effectively and efficiently to avert any losses that may occur.

For banks to be able to use their operational risk management policies and guidelines to compete they need to first identify their critical success factors. From the literature review the critical success factors of banks are staff, strength of network, primary position in domestic market, image and reputation, product differentiation, internal guidelines and policy on operational risk management and technology. From the survey all the respondents indicated that all the seven are perceived to be a source of competitive advantage for their banks with the highest being technology and staff. Human resource is critical to the survival and growth of all institutions. Banks cannot operate without human resources. In this technological era banks compete for customers by coming up with electronic products.

The outcome of this study indicates that operational risk management indeed has a direct bearing on the relationship between critical success factors and competitive advantage. The following elements (staff, technology, primary position in domestic market, product differentiation, internal procedures and guidelines on ORM, Networking etc) are all positively and significantly correlated with one another. All these factors come into play in the day to day activities of banks. Banks cannot operate effectively without their staff because they are the face of the business, staff needs the technology to function, and the products are what bring staff in direct contact with customers. Banks also rely on the relationships that they have with other companies to secure their business transactions. All of these will affect the primary position that the banks have on the domestic market which will impact on their image and reputation on the market. The findings thus prove that effective management of operational risk will eventually drive banks towards a stronger and solid relationship between critical success factors and competitive advantage in the industry.

Respondents perceived all these elements to be sources of competitive advantage for their banks. This indicates that all the seven are interrelated meaning that for banks to gain competitive advantage they need to pay particular attention to all of them. From the literature and earlier discussions, all these elements are inherent in operational risk and for banks to be able to achieve competitiveness through them there is the need for a critical look at each element and how each can contribute to collectively ensure that competitive advantage is gained. Management of operational risk is the responsibility of staff at all level in banks therefore banks must ensure that they recruit and retain staff with the appropriate expertise, skills and experience. Responsibilities should be well communicated to staff and regular and adequate training must be provided for them to be adept in their roles.

Technology is a vital tool in all bank activities, as customer become more aware and demanding, banks must ensure that they continuously improve upon their technology since all banks compete for the same customers. To ensure that they gain competitive advantage they must ensure that funds are made available for their development of hardware and software infrastructure.

Banks cannot manage their operational risk activities without having in place internal guidelines and policies on ORM. These policies and guidelines must be made known to all staff. This mean that banks must have an effective communication system whereby staff are informed on a regular basis on operational risk issues. The policies and guidelines must be easily understood and made available to all staff.

Customers are attracted to banks based on their products and services. For banks to be able to gain competitive advantage they must ensure that they are continuously developing new products and services that meet the expectations and demands of customers. Bank customers have different demographics and products should be differentiation to ensure that all categories of customers are well catered for. The primary position of banks in the domestic market can also be a source of competitive advantage. Position in the market assures both customer and investors of the quality and the standard of banks.

Risk management in general is not a one-off activity. As the emphasis shift from 'making money to not losing money, effective operational risk management has become increasingly important for banks.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

This chapter provides concluding statements on the Ghanaian Banking Industry's operational risk condition, the adequacy of its operational risk management framework in handling the operational risks being encountered and how operational risk management can be a major source of competitive advantage in the industry. The conclusions are supported by a summary of the findings from the analysis. The chapter also contains some recommendations aimed at ensuring that banks manage their operational risks effectively and efficiently to ensure they gain competitive advantage.

5.1 Summary of Findings

From the analysis, operational risk management is indeed quite new in the Ghanaian banking industry. However, banks have come to realize that there are risks inherent in their day to day activities which when not managed will cause them to lose significantly (loss of customers, money and reputation). As a result the Bank of Ghana regulation for banks to be fully compliant with the Basel II directive of setting aside some capital to cater for operational issues when they occur, and the urge to stay ahead of competitors in this era of increased competition, banks are gradually embracing operational risk management. Operational risk management is the responsibility of everyone in the organization including the board of directors and as such banks are aligning their strategies and objectives to operational risk management. In this competitive environment banks are becoming increasingly aware of their critical success factors and how these can help them gain competitive advantage in the industry. There are a number of sources to competitive advantage for banks (i.e. staff, strength of network, primary position in domestic market, technology, product differentiation, image and reputation and internal guidelines and policy on operational risk). These sources play a collective role ensuring that banks stay ahead of their competitors. Each of these sources play a role in operational risk and banks are realizing that they need to take a critical look at each of them by assessing the role they each play in their day to day activities in ensuing that they gain competitive advantage.

Aligning these findings to the hypotheses of the research, which assumed that;

- Operational risk has an impact on the Ghanaian Banking Industry.
- With a good operational risk management framework in place Banks will be able to gain an advantage over their competitors,

It is evident that indeed the two hypotheses have been established from the findings.

5.2 **Conclusion**

As operational risk management efforts improve and gain both the full support of board and management of banks, they are increasing becoming valuable to bank activities. The concept of operational risk management was initially conceived to support regulatory requirements but these efforts can also be leveraged and aligned with critical success factors to ensure that organizations gain competitive advantage. For banks to be successful, this alignment must be based on a clear vision of the potential benefits of effectively managing operational risk.

The study provides additional support for the importance of operational risk in the Ghanaian banking industry. The findings support the view that operational risk management has a direct linkage to banks' critical success factors which can lead to competitive advantage in the industry.

5.3 Recommendations

The following recommendations are being made with the aim of helping to improve the operational risk management system in banks and thus making them more competitive.

i. Banks should link their operational risk management activities to their business objectives and identify the potential hurdles that hinder their competeveness. This will ensure the day to day management and control of operational risk.

ii. There should be an effective operational risk management policy and effectiveness of the systems of internal control within the areas of their business. Management must ensure strict adherence to this policy and ensure that any exceptions are appropriately reported and resolved.

iii. Board of Directors of Banks should be actively involved in operational risk management They should approve the overall business strategies and significant policies of their institutions, including those related to managing and taking risks and must ensure that lines of business are managed and staffed by personnel with knowledge, experience and expertise that are consistent with the nature and scope of the organizations activities.

iv. Awareness must be created on the need to identify, evaluate, monitor, control and report operational risk issues in accordance with the strategies and policies of banks in ensuring the adequacy of capital against operational risk.

v. Banks should act diligently and expediently to meet the Bank of Ghana Basel II compliance deadline of 2012 and have in place strategies for Basel Compliance.

vi. Although risk management is the responsibility of all staff at all levels, there must be an explicit allocation of risk management responsibility among senior managers to ensure management accountability for risk control. Banks must make risk visible, measurable and manageable and ensure a meaningful risk culture throughout all processes and activities.

vii. There are no set rules for Operational Risk Management framework that are applicable to every bank. Thus each bank requires a framework that is specific and custom made to suit its own operating environment. Ultimately, the Operational risk framework should not merely be Basel-compliant; it should also provide banks with mechanisms for improving overall risk culture and behavior towards operational risk management. Understanding risks will lead to better decision making and reflect in our performance.

viii. Operational risk must be effectively monitored continuously with new information documented. This document must be updated from time to time as banks' become more experienced in operational risk issues.

ix. To stay ahead of the competition at all times, banks must ensure there is a continuous monitoring process to ensure the integrity of their operational risk management controls and systems.

x. Finally, with the growing demand of customers for quality products and services and investors looking out for high growth in earnings, further research needs to be undertaken to extensively delve into operational risk and how Ghanaian banks can continuously assess and quantify operational risk activities in order to be able to effectively manage it.

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APPENDIX I

KWAME NKRUMAH UNIVERSITY OF SCIENCE AND TECHNOLOGY

(INSTITUTE OF DISTANCE LEARNING)

This is a research being conducted in partial fulfillment of the requirement for the award of Master of Business Administration (MBA) on "**OPERATIONAL RISK MANAGEMENT AND COMPETITIVE ADVANTAGE IN THE GHANAIAN BANKING INDUSTRY**.

The purpose is to identify how relevant operational risk is to the banking industry and whether operational risk management can be a source of competitive advantage within the industry The questionnaire is in 3 sections 1) Risk in banking industry; and 2) Objectives/Strategies on operational risk management in your bank; and 3) Perceived competitive advantage in your bank.

Respondents are assured of confidentiality and anonymity of the information they provide. You are further assured that any information you provide is purely for academic purposes.

INSTRUCTION: Please tick where applicable and supply details where required.

Questionnaire: Section 1 – Risk in the banking industry

1.1 How relevant are the following types of risks in your Bank? (Please tick only one option for each type)

Type of Risk	**Not at all**				**Very relevant**
	1	**2**	**3**	**4**	**5**
Environmental Risk					
Market Risk					
Operational Risk					
Credit Risk					
Legal Risk					
Liquidity Risk					
Reputational Risk					

1.2 How regularly are the following types of risk being formally assessed and quantified? (Please tick only one option for each type)

Type of Risk	Annually	Semi-Annually	Quarterly	Monthly	Bi-Monthly	Weekly	Daily
Environmental Risk							
Market Risk							
Operational Risk							
Credit Risk							
Legal Risk							
Liquidity Risk							
Reputational Risk							

1.3 How regularly are the following types of risk being formally managed? (Please tick only one option for each type)

Types of Risk	Annually	Semi-Annually	Quarterly	Monthly	Bi-Monthly	Weekly	Daily
Environmental Risk							
Market Risk							
Operational Risk							
Credit Risk							
Legal Risk							
Liquidity Risk							
Reputational Risk							

Questionnaire: Section 2 – Objectives/Strategies on Operational risk management

2.1 Operational Risk is being defined under the Basel 2 Accord as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. A minimum regulatory capital of 8% is to be set aside for every exposure under this heading. Do you consider this risk as relevant to the Ghanaian banking industry? (Please circle only one)

Yes **No** **I do not know**

2.2 How important is current risk management practices in your bank?(Please circle only one)

Not at all **Very Important**

1 **2** **3** **4** **5**

2.3 Your bank is able to allocate appropriate resources in support of operational risk management policy and practice. (Please circle only one)

Not at all **Very Important**

1 **2** **3** **4** **5**

2.4 How important is effective operational risk management to the achievement of your bank's objectives? (Please circle only one)

Not at all **Very Important**

1 **2** **3** **4** **5**

2.5 To what extent has your bank developed a close link between its strategic objectives and management of operational risk (e.g. operational risk identification is conducted during strategic planning process)? (Please circle only one)

Not at all **Significantly**

1 **2** **3** **4** **5**

2.6 Does your bank have any internally developed operational risk management procedures or guidelines?

Yes **No**

Questionnaire – Section 3: Perceived Competitive advantage of your bank

3.1 To what extent does your bank perceive operational risk management as a source of competitive advantage? (Please circle only one)

Not at all				**Significantly**
1	**2**	**3**	**4**	**5**

3.2 To what extent do your perceive that operational risk loss will impact on your bank's competitive advantage?(Please circle only one)

Not at all				**Significantly**
1	**2**	**3**	**4**	**5**

3.3 What are the perceived sources of competitive advantage in your bank? (Please tick all that apply)

a. Staff ☐
b. Strength of network (Relationship) ☐
c. Primary position in domestic business ☐
d. Image and Reputation ☐
e. Product differentiation ☐
f. Internal guidelines and policy on operational risk management ☐
g. Technology ☐
h. Others (Please specify) ……………………………………………………………… ☐

3.4 How important is Staff as a source of competitive advantage in your bank? (Please circle only one)

Not at all				**Very Important**
1	**2**	**3**	**4**	**5**

3.5 How relevant is strength of network as a source of competitive advantage in your bank? (Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.6 How relevant is primary position in domestic business as a source of competitive advantage in your bank? (Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.7 How relevant is product differentiation as a source of competitive advantage in your bank?(Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.8 How relevant is image and reputation as a source of competitive advantage in your bank?(Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.9 How relevant is good operational risk database as a source of competitive advantage in your bank?(Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.10 How relevant is internal operational risk control policy as a source of competitive advantage in your bank?(Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.11 How relevant is senior management's support on operational risk management as a source of competitive advantage in your bank?(Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.12 How relevant is being a pioneer in operational risk management in the industry as a source of competitive advantage in your bank?(Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

3.13 How relevant is technology seen as a source of competitive advantage in your bank? (Please circle only one)

Not at all				**Very Relevant**
1	**2**	**3**	**4**	**5**

Thank you for completing the questionnaire.