

**ST.MARY'S UNIVERSITY  
SCHOOL OF GRADUATE STUDIES**

**PERCEPTION OF BANKERS TOWARDS  
THE CHALLENGES AND OPPORTUNITIES  
OF OUTSOURCING PRACTICES IN THE  
BANKING SECTOR IN ETHIOPIA**

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**BY  
ROBEL SIYOUM  
ID NO. SGS/0112/2004**

**SEPTEMBER 2013  
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**A THESIS SUBMITTED TO ST.MARY'S UNIVERSITY, SCHOOL  
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**ST.MARY'S UNIVERSITY  
SCHOOL OF GRADUATE STUDIES  
FACULTY OF BUSINESS**

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## LIST OF ACRONYMS

AB	Abay Bank
AIB	Awash International Bank
BFI	Banking and Finance Industry
BPO	Business Process Outsourcing
CBE	Commercial Bank of Ethiopia
CN	Commercial Nominees
DBE	Development Bank of Ethiopia
FM	Facility Management
HRM	Human Resource Management
ISM	Information System Management
IT	Information Technology
ITO	Information Technology Outsourcing
SD	Standard Deviation
UB	United Bank

## ABSTRACT

*This study was conducted to examine the outsourcing practices in banking sector of Ethiopia. A descriptive case study was employed to achieve the goal of this research. Two government banks and three private banks were selected as samples and 100 participants from three areas of business process (Human Resource Management, Facility Management and Information technology business process) were involved on the study. In order to get relevant data from the target population questionnaire and interviews were used. The questionnaire was administered to the experts, senior officers and managers and the interviews were conducted with the senior managers of the five sampled banks. The collected data were analyzed using frequency, mean, standard deviation, and percentage values. The findings generally indicate that outsourcing practices in Ethiopian banks is at its infant stage dominated by outsourcing very few noncore businesses which are security, cleaning, and maintenance services. The major motivations for outsourcing are management convenience and focus on core business. Moreover, cost saving was found to be important motivator but not major reason for outsourcing. Achieving focus on core business, cost shifting and management convenience are given high expected benefits of outsourcing. Data security and data confidentiality risks are highly expected risks of outsourcing. The major challenge for Ethiopian banks to outsource is lack of qualified and professional service provider from the market. Generally finding indicates that outsourcing strategy has a potential to grow in the future. Based on findings of the study banks are recommended to make a serious risk analysis of outsourcing and to incorporate efficiency variables on the outsourcing contracts to monitor outsourcing strategy effectiveness. Service providers also recommended to focus on growth of business value not cost reductions on their offers because clients are tend to value quality than pure cost savings.*

*Key words: outsourcing, perception, Business process outsourcing, Banks*

## CHAPTER ONE

### INTRODUCTION

#### 1.1 Background of the study

One of the current business strategies to have emerged for many organizations has been the growing importance of outsourcing (McIvor, 2000). Outsourcing is defined as having work that was formerly done inside the organization performed by an external organization (Beaumont and Sohal, 2004). The practice of outsourcing is not a new phenomenon; since firms have always made decisions on buy or made. The advancement of information technology and globalization make easy to outsource activities which are noncore and less competitive business functions. The drive for greater efficiency and continuous cost reduction has forced many organizations to outsource activities which traditionally were carried out in-house. For this reason, organizations can focus on their core competencies, which contribute most to a sustainable competitive advantage (Gewald, 2010).

The growth of outsourcing market is increasing in types that moves from activities that are noncore to the organization such as cleaning, catering and security, to include core areas of activity such as design, manufacture, marketing, distribution and information systems with almost the entire value chain open to the use of outside supply (McIvor, 2000).

The global trend of outsourcing is growing fast in terms of complexity and market whereas the growth of outsourcing in Ethiopia is at its infant stage. It is dominated by non-core functions like Security and Janitorial service (Meresea, 2007). The banking environment in Ethiopia has, for the past decades, undergone many regulatory and financial reforms. These reforms have brought about many structural changes in the banking sector of the country and have also encouraged private banks to enter and expand their operations in the industry. Despite these changes, currently, the banking industry in Ethiopia is characterized by operational inefficiency, little and insufficient competition and also can be distinguished by its market concentration towards the big government owned commercial bank (Lelissa, 2007 cited in Abera, 2012).

In the context of the above discussions, the purpose of this study is to assess challenges and opportunities of outsourcing practices in Ethiopian banking industry.

## **1.2 Statement of the problem**

Firms in this dynamic global economy are expected to be highly competitive in every aspect. To be competitive they need modern management practices that go with the current organizational culture and global market. One of current modern management practices that are growing rapidly across the globe is outsourcing. It is becoming more sophisticated and complex (Beaumont and Sohal 2004). The trend of outsourcing started from 1980 with the basics information technology outsourcing to non core business process and now reached to the more strategic core business process of organizations (Schniederjans et al., 2007 cited in Kumar and Natarajan, 2011). Several global research agencies have reported that worldwide, outsourcing engagements have been growing and will continue to grow consistently both in terms of number of contracts and their average contract value. The global outsourcing market in terms of total contract value has grown to US\$1.3 trillion in 2007 (Global Outsourcing 100 Index 2011 cited in Kumar and Natarajan, 2011).

Various empirical as well as theoretical studies of outsourcing list benefits of outsourcing based on various theoretical explanations. They indicate that outsourcing is an efficient tool for using the technology and capital resources of firms for competition in fast changing market environment. It also leads to costs savings and enhances the quality of services (Kim et.al, 2007). External organizations can often provide greater economies of scale, flexibility, and levels of expertise for overhead services that virtually any company can achieve internally. In the mean time the outsourcer firm may lose its control over the outsourced service and it may bear risk of becoming dependent on the service provider company (Maynard, 2006 cited in Meresea, 2007).

According to Kumar and Natarajan, 2011, several studies in financial services sector pertaining to outsourcing show a gradually growing trend in outsourcing, both in terms of nature and scope of activities outsourced, and also emphasize that outsourcing is an inevitable and critical aspect of financial institutions to survive in a rapidly changing business environment. In fact, industry

research indicates that Banking and Financial Services Industry has been the largest sector user of outsourcing services worldwide, next only to manufacturing (Ackermann, 2003 cited in Kumar and Natarajan, 2011).

In Ethiopia, banks are more of driven by modern management practices. However, the practice of outsourcing as a strategy is not well developed (Meresea, 2007). This variation attracts the researcher to undertake a research with the objective of evaluating the current practice and future potential of outsourcing in the country's banking industry. Hence, the financial services sector was a logical choice to focus on. Thus, the research will answer the following questions:

1. What is the trend of outsourcing in Ethiopian banking industry?
2. Which activities of the banks are outsourced?
3. What are the perceptions of bank management toward benefits and risks of outsourcing?
4. What is the significance of outsourcing as a business strategy?
5. What are the major obstacles to outsource?

### **1.3 Objective of the study**

The general objective of the paper is to find out challenges and opportunities of outsourcing practices in banking industry of Ethiopia. The specific objectives are:

- To assess overall outsourced activities by the banks.
- To find out the perception of managers on benefits and possible risks of outsourcing.
- To find out barriers for outsourcing.
- To evaluate the importance of outsourcing as a business strategy.

### **1.4 Hypothesis**

The study has three sets of hypothesis which are related with association of different sets of variables. These are:

1.  $H_o$ : There is no relationship between the perceived benefits of outsourcing and criticality of outsourcing as business strategy.

$H_1$ : There is a relationship between the perceived benefits of outsourcing and criticality of outsourcing as business strategy.

2.  $H_o$ : There is no relationship between the perceived outsourcing risks and criticality of outsourcing as a business strategy.

$H_1$ : There is a relationship between the perceived outsourcing risks and criticality of outsourcing as a business strategy.

3.  $H_o$ : There is no relationship between the perceived roadblocks of outsourcing and criticality of outsourcing as a business strategy.

$H_1$ : There is a relationship between the perceived roadblocks of outsourcing and criticality of outsourcing as a business strategy.

### **1.5 Significance of the study**

The practice of outsourcing in Ethiopia and awareness among the society is not well developed. In the academic areas research related to outsourcing focusing on Ethiopia is few. Hence the study aims to create awareness about outsourcing for different stakeholders of the financial industry specifically for employees and managements of the banks and also for business persons and scholars. Furthermore, this research can serve as stepping stone for other research in similar area.

### **1.6 Delimitation of the study**

The study is conducted in the banking sector of Ethiopia in the areas of outsourcing as a business strategy. The research covers five banks as a sample from nineteen banks that are operating in Ethiopia. The data were gathered from senior managements and experts of banks in the area of

information system, human resource and facility management. Due to time and budget constraint outsourcing service supplier's perspectives are not entertained in this study.

### **1.7 Operational definitions**

***Back sourcing:*** - work that was outsourced is taken back in-house (Beaumont and Sohal, 2004).

***Business Process Outsourcing (BPO):*** - the delegation of one or more entire business process to an external service provider (Gewald and Dibbern, 2005).

***Facilities Management:*** - the integration of processes within an organization to maintain and develop the services which support and improve the effectiveness of its primary activities (Borisova, 2011).

***Facilities Management Outsourcing:*** - An outsourcing solution in which the customer entrusts to an external services provider, the responsibility for operations and maintenance of one or more facilities (Borisova, 2011).

***In-sourcing:*** - applying outsourcing's discipline to internal suppliers, often having them competes with external suppliers (Beaumont and Sohal, 2004).

***Offshore Outsourcing:*** - the transfer of organizational activities carried out locally to product and service providers in other countries (Bojan and Lewandowski, 2010).

***Out-tasking:*** - indicate work being done outside the organization, but the organization retaining full control over the operation over how it is to be done. The vendor has no discretion and performs a programmable task (Beaumont and Sohal, 2004).

## **1.8 Organization of the study**

The research work is organized in five chapters. The first chapter is an introductory part. The second chapter concentrates on literatures in relation to the subject matter of the paper. The third chapter discussed about the methodology of the study. The fourth chapter is all about results and discussion. The last chapter bring the study to an end through conclusions and recommendations.

## CHAPTER TWO

### LITERATURE REVIEW

#### 2.1 Practices of outsourcing

Outsourcing traced back to the industrial revolution of England in 1700 (Beaumont and Sohal, 2004). But its significance and its fashionable way of solving some business problems are getting more attention as a business strategy is increased in recent years. It is initially used primarily for information technology (Ibid, 2004). Now a wide variety of business process is outsourced. The use of outsourcing is becoming more sophisticated; more organizations are outsourcing their business processes. Cleaning, IT, catering and security are well-known examples of activities that are frequently outsourced (Ibid, 2004).

##### 2.1.1 The global trend

With the global telecommunications, transportation and other infrastructure now well established and consistently reliable, more outsourcing initiatives are under taken beyond in shore and near shore service providers to include shifting work to international providers (Duening and click, 2005). Oshri et al. PP1, (2009) on title, Global Outsourcing Recent trends and issues, discuss the global trends of outsourcing. They summarized the global trend as follows:

*There will be a continuing rise in outsourcing revenues for global outsourcing, with BPO overtaking ITO within five years. India will continue to dominate the outsourcing market but its role will change. China gives out promise but will still struggle to achieve scale in Western European and North American markets. Emerging country competition will intensify. Near-shoring will be a strong trend. Outsourcing, by offering a potential alternative, will help discipline in-house capabilities and service. Knowledge process outsourcing will increase as emerging countries move up the value chain. Outsourcing successes and disappointments will continue as both clients and suppliers struggle to deal with a highly dynamic set of possibilities.*

### **2.1.2 Trends of outsourcing in Ethiopia**

In order to gather the trends of outsourcing in Ethiopia there is lack of research works. However according to one master's thesis research that was done by Meresea, (2007) on outsourcing practice in Ethiopia, the use of outsourcing in Ethiopia is very low and limited with the exception of the use of some Non-core functions like Security service and Janitorial service. The most outsourced business functions listed are maintenance service, janitorial service, security service and information technology. Conversely, Accounting and Administration services are mentioned less outsourced by Ethiopian organization. The main reasons for not outsourcing are organizations fear of loss of confidential information and loss of control. In addition, the organizations suspect that the external service providers are not loyal to them (Ibid, 2007).

### **2.2 Outsourcing practice in financial institutions**

The outsourcing strategy has shifted from product and service focus to that of differentiation and speed to market. Several studies pertaining to outsourcing in the financial services sector show a gradually growing trend in outsourcing, both in terms of nature and scope of activities outsourced, and also emphasize that outsourcing is a critical aspect of financial institutions to survive in today's business environment (Federal Reserve Bank of New York, 1999).

The justification for outsourcing activities, such as cash management, research and business analytics, and other processes that otherwise are considered core to the banking business, lies in the argument that these activities, though essential to the bank, do not provide a unique competitive advantage. This implies that those activities, where a bank can do better than its competitors, and which generates a competitive advantage, are retained in house and the rest are outsourced (Chris, et.al. 2004 cited in Prasad et.al., 2011).

Financial institutions have outsourced activities such as information technology, accounting, audit, electronic funds transfer, investment management, and human resources. According to Federal Reserve Bank of New York (1999) citing published reports, thirty-nine percent of all

U.S. banks and thrifts outsourced at least some processing activities in 1998 and the most frequently outsourced activity is some aspect of information technology. Next in importance is BPO, such as treasury operations, internal audit and human resources. BPO is the emerging area of growth since it facilitates financial institutions' reengineering of core business processes (Federal Reserve Bank of New York, 1999).

### **2.3 Types of outsourced services**

The general trend in all sector shows that companies first outsource those business functions that are noncore for the organizations with the aim of reducing costs and focusing on core functions. Among non core activities call centers, janitorial services, maintenances and information technology are commonly outsourced. Recently more and more business processes are being outsourced from partially outsourcing a business process to completely outsourcing the total work of business process. Various researches illustrate that Information technology; human resource and facility management are among the most outsourced business process.

#### **2.3.1 Information technology outsourcing**

Outsourcing is a trend that is more common in information technology for services that have usually been regarded as intrinsic to managing a business. In some cases, the entire information management of a company is outsourced, including planning and business analysis as well as the installation, management and servicing of the network and workstations (Nag, 2004).

As financial processes are almost fully digitizable, the banking and finance industry heavily relies on information technology. Accordingly, IT has been a strong driver of developments in the BFI with ATMs being a renowned example. Powerful information systems have made the processing of large transaction volumes possible, at the same time enabling new E-Commerce products and services like online banking. Driven by cost pressure and new competitors, outsourcing IT together with the relevant business processes is a promising way to focus on core competencies and to restructure the corporate value chain.

The benefits of IT outsourcing in the BFI is well understood. However, the risk of outsourcing is not well known. This raises questions about the impact of risk facets such as financial, strategic, performance and social risks on outsourcing decisions in firms Gewald et. al (2006). Advances in IT have provided banks with the opportunity to use outsourcing as a means to reduce costs and focus on core competencies (Ibid, 2006).

### **2.3.2 Human resource outsourcing**

The decision of HR outsourcing is contingent upon factors like flexibility, availability of adequate resources, affordability, and acceptability (openness to information-sharing) etc. According to analysts, companies usually cite cost reduction as the most crucial reason for HR outsourcing. As companies were discussing how to cut costs in the face of an economic downturn, many look at outsourcing for some of their HR processes. However, some analysts argue that by outsourcing major HR activities, the number of HR jobs is decreasing, others feel that on the contrary by outsourcing these kinds of repetitive and administrative jobs, higher-level HR professionals get the time they need to tackle strategic workforce challenges (Seth and Sethi, 2011).

HR services are among the key elements in the enlarging outsourcing game. Recognizing the fact that senior management needs to get out of mundane day to day processing work and focus instead on strategic planning, core competencies, customer satisfaction and decision making, a number of large companies, across globe have begun selecting for outsourcing of their HR services. Some of the functions most commonly handed over to outside providers include payroll, benefits administration, background checks, drug testing, recruiting and training. Even small companies turn to outside services to help with such everyday jobs (Seth and Sethi, 2011).

### **2.3.3 Facility management outsourcing**

Facility management is one of noncore business process activities commonly outsourced. Facilities and properties maintenances and procurements are the main areas of facility management services. Facility Management can be summarized as creating the optimal

environment for the organization's primary functions, taking an integrated view of the business infrastructure, and using this to deliver customer satisfaction and best value through support for and enhancement of the core business (Borisova, 2011).

In many organizations Facility Management function is new function that provides a connection between the core activities and the facility activities. Facility Management function can be fulfilled by a facility manager internally or by a facility manager of an external service providers (Borisova, 2011). Today the trend is that many services related to Facility Management, transferred to the outsourcing. In the international market there are companies that specialize in transportation logistics, cleaning, archiving, preservation, security, etc.

The reason why Facility Management services are given to the outsourcing is enormous costs that are hold by the owner, if performed internally. Facility Management companies can professionally optimize and significantly reduce these costs (Tswetkow 2011 cited in Borisova, 2011).

## **2.4 Theoretical background and concept of outsourcing**

### **2.4.1 Theories in outsourcing**

Various theories are used by scholars for explanations of why outsourcing occurs. Many of outsourcing arguments have a basis in economic theories. Transaction cost theory which typically frames outsourcing as a decision about drawing firm boundaries or as vertical integration, offers economic perspective of outsourcing (Ang and Straub 1998). McIvor (2008) on the study of general reviews of outsourcing related research identified the "top-10" list of ten theories which have come across most frequently on outsourcing related research, these are:

- (1) Transaction cost theory (Coase, 1937; Williamson, 1975, 1985).*
- (2) Resource-based view (Penrose, 1959; Richardson, 1972).*
- (3) Principal agent theory (Ross, 1973; Jensen and Meckling, 1976).*
- (4) Vertical integration theory (Bain, 1968; Grossman and Hart, 1986).*

- (5) *Strategic management (Quinn and Hillmer, 1994).*
- (6) *Evolutionary economics (Nelson and Winter, 1982; Mahnke, 2001).*
- (7) *Relationship market/view (Berry, 1983; Sommer, 2003).*
- (8) *Industrial economics (Porter, 1980).*
- (9) *Strategic alignment theory (Henderson and Venkatraman, 1990).*
- (10) *Core competence theory (Prahalad and Hamel, 1990)*

#### **2.4.2 Outsourcing decision framework**

Outsourcing is often combined with competitive tendering for the contract under which the goods and services are to be provided. Businesses of all types, both large and small, have been outsourcing activities for many years and have benefited from it; they know the value that outsourcing brings to their organization, as a tool to enhance and enlarge the business. Organizations that have repeatedly used outsourcing over a substantial period know that to sustain the positive benefits that it brings to the organization, it is also important to have a well managed plan of action for the outsourcing process. This includes deciding which activities or tasks to outsource, which companies should be hired to perform these tasks, how to manage the outsourced business process, how to agree on payment terms, and how to ensure that the desired results are achieved (Beaumont and Sohal, 2004).

Outsourcing is a hierarchical sequence of decisions. The fundamental decision is whether or not to outsource a business process or function. Outsourcing decisions can be complex because modern organization's applications tend to be integrated with each other, sensitive; it may be difficult to separate and outsource a single application. The criteria used to evaluate outsourcing decisions may be multidimensional and intangible; besides difficult to estimate cost savings, the firm must consider intangible effects such as freeing up managerial time and possible dependence on the vendor (Beaumont and Sohal, 2004).

Kremic et. al (2006) mention that an empirical survey of BFI managers covering 90% of the cumulated German BFI balance sheet, it is shown that perceived risk does indeed have a

significant impact on managers' attitudes towards BPO and that these attitudes strongly influence the outsourcing decision.

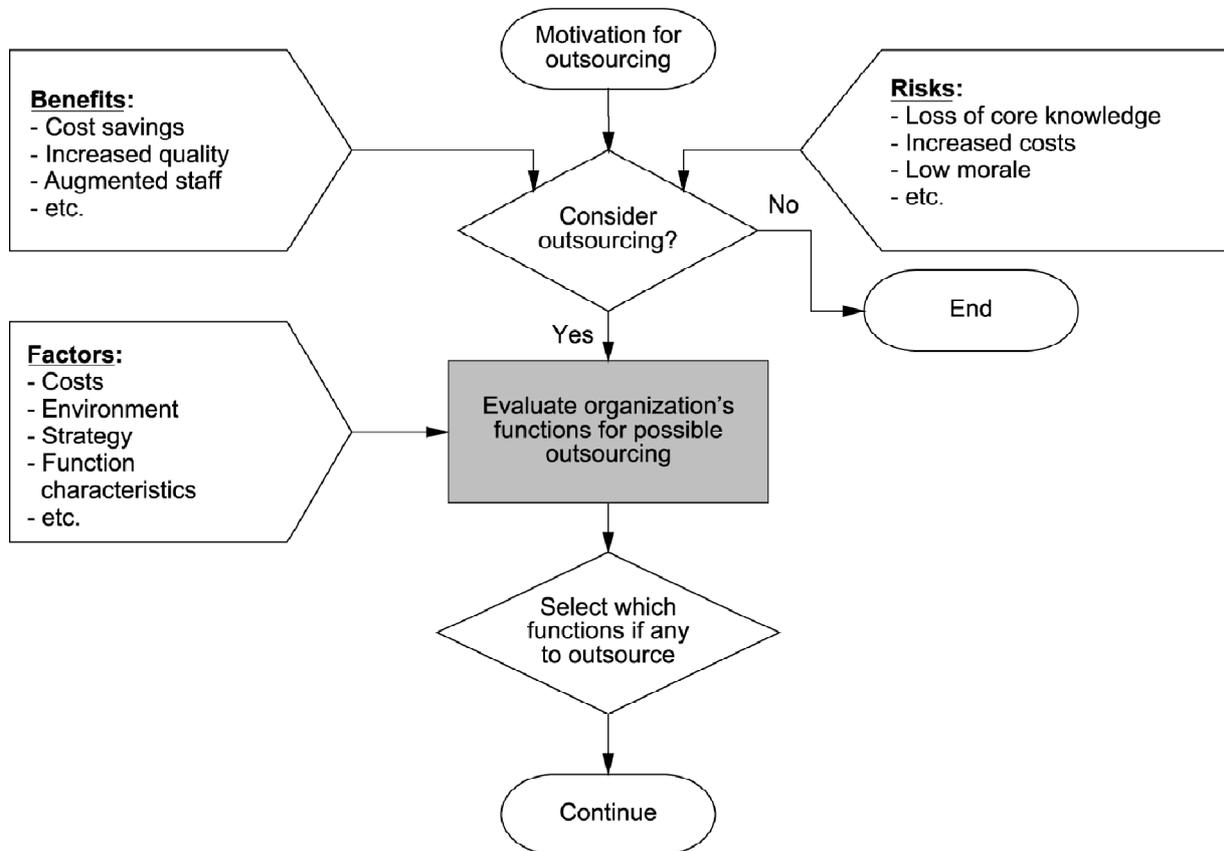


Figure 1: Outsourcing decision framework. Adapted from Kremic et. al (2006)

## 2.5 Motivations of outsourcing

Companies that are Successful in practicing outsourcing leverage their capabilities and investments by exploiting three areas of functional activities performed in house by outsourcing. These activities are complementary, integrative, or duplicative activities scattered throughout the company; in which outsiders have greater expertises or capabilities for innovation. Therefore, by outsourcing noncore activities for vender organizations, clients can focus on their core activities that give them competitive advantage and improve overall performance (Kim and Won, 2007 cited in Kremic et. al., 2006).

There are motivations for outsourcing in companies. They can be categorized in to three: cost, strategy, and politics. Whereas there may be three categories, outsourcing activities are mostly to be initiated by elements from all three categories. Cost and strategy motivations commonly drive outsourcing by private organizations. Political agendas often drive outsourcing by public organizations (Kakabadse and Kakabadse, 2000a, cited in Kremic et. al., 2006).

### **2.5.1 Cost Driven Outsourcing**

Saving cost is the major reasons for outsourcing practice for many organizations. Cost saving can occur when suppliers' costs are low enough that even with added overhead, profit, and transaction costs suppliers can still deliver a service for a lower price. Service provider can able to deliver the service with low cost than the client with the mechanisms of Specialization and economies of scale Kremic et.al. (2006). A desire to save indirect costs may also drive outsourcing. Outsourcing allows having fewer employees that requires less infrastructure and support systems which may result in a more efficient organization. Some organizations outsource to achieve better cost control while others try to shift fixed costs into variable costs (Kremic et. al., 2006).

Even though organizations may outsource for cost related reasons, increasing evidence on literatures shows that cost savings have been overestimated and costs are sometimes higher after outsourcing. In addition to not realizing the costs that originally drove the outsourcing initiative, there are also some additional indirect costs like contract monitoring and oversight, contract generation and procurement, intangibles, and transition costs and social costs like low morale, high absenteeism, lower productivity etc. that may be incurred. The literature shows that significant savings can result. However, savings are not a given. Apparently the effects of outsourcing on an organization's cost are not yet fully understood and perhaps the variables and their relationships are more complex than expected Kremic et.al. (2006).

### **2.5.2 Strategy driven outsourcing**

Another mostly cited driver for outsourcing is strategic issues such as core competence and flexibility. Because of intense competition, organizations are forced to redirect scarce resources where they make the greatest positive impact, namely the organization's core functions. Outsourcing is to allow the organization to better focus on its core competencies. Other strategy issues which encourage the consideration of outsourcing are restructuring, rapid organizational growth, changing technology and the need for greater flexibility to manage demand swings (McIvor, 2000). Organizations need to react quicker to customer requirements and outsourcing is seen as a means to accomplish it (Kremic et. al., 2006).

### **2.5.3 Politically driven outsourcing**

Political motive for outsourcing shown in public organization since most of their issues may be more social than economic. Other factors that may be drive outsourcing by public organizations include public organizations are sometimes perceived as inefficient and bureaucratic, political candidates may promote outsourcing ideas, particularly at election time, to demonstrate their willingness to make positive changes, for better accountability in public organizations, the agendas of elected officials, public opinion, and current national or international trends (Avery 2000, cited in Kremic et.al., 2006). Manager's preference to divest of troublesome functions is another major reason to outsource. In summary, there is enough evidence in the literature to suggest that outsourcing by public organizations may be initiated for reasons quite different from private industry (Kremic et.al., 2006).

## **2.6 Advantage and disadvantage of outsourcing**

Outsourcing is used because it gives advantages to the organization. However it brings also a risk for the organization. Ang and Straub (1998) cited different studies and forwarded that a cost advantage by hiring outsiders to perform certain services and produce certain products is one of the most commonly cited reasons for outsourcing by managers.

If the organization has accumulated specific assets and skills peculiar to the process then in house processing should be considered (this is especially so if the in-house operation, through experience or economies of scale, is cheaper and/or provides higher quality than potential vendors). If the internal operation is inefficient or distracts management, an outsourcing partnership should be considered. The partner and client will cooperate by using their skills, experience, and assets to optimize the process and adapt it to changing business conditions (Beaumont and Sohal, 2004).

According to Beaumont and Sohal (2004) a business process is strategic if it gives a unique competitive advantage. If the business process is strategic, the organization will probably not want to become dependent on or share sensitive knowledge with vendors who might supply the client's competitors; the normal option is in sourcing. However, a strategic business process may have several aspects some of which can be outsourced. For example, although customer relationship management (CRM) may be critical and strategic, it may be appropriate to outsource call center operations while retaining in house authorship of operators' scripts and responsibility for databases.

Pressures to outsourcing in the goal of companies that aggressively outsource most functions are to enhance competitiveness by achieving a higher return on assets through less capital commitment and increasing the ability to adjust quickly to a changing environment through less commitment to in-house resources.' Their motto is: do more with less. Outsourcing is motivated by growing pressures on management to remain competitive by accomplishing more with fewer resources at a faster pace. Competitive pressure is a constant driver to increase efficiency. Organizations have been, or are being, restructured, downsized, and reengineered in a relentless attempt to achieve a state of efficiency, effectiveness, and agility expected to deliver increased productivity. In order to do more with less, a company must focus its limited resources on those activities that are essential to its survival and must leverage activities that are peripheral. The result is a greater use of partnerships, collaborations, and simple buying to substitute for in-house capabilities.

### **2.6.1 Advantages of outsourcing**

Given that outsourcing will be a natural outgrowth of globalization and fast changing technology for many companies in the world, those who anticipate and manage these changes strategically, the gains can be enormous (Zhu et.al, 2001). Researches shows that there are various reasons to outsource that include reduced costs, enhanced performance, an ability to access superior expertise and industry best practices, and a desire to devote scarce human resources to core businesses (Federal Reserve Bank of New York, 1999). The following elaborate the major once

**Reduce and control operating costs:** - A vendor may provide better performance at a lower cost than in houses because of economies of scale, specialization and tactical focus. Cost savings may be secured by converting fixed costs to a variable cost structure to accommodate fluctuations in labor and equipment needs and by purchasing services at a fixed cost per transaction, a client can avoid financial uncertainty. Additionally, outsourcing can provide immediate access to expertise and best business practices that may be too expensive to build internally or hire particularly in areas such as technology (Federal Reserve Bank of New York, 1999). Outsourcing reputedly reduces IT costs. Vendors convince firms by claiming to cut costs by 10-50 percent and Economies of scale can lower costs (Lacity and Hirschheim, 1993 cited in Beaumont and Sohal, 2004).

**Concentration on core activities and competencies:** - Managers should apply their experience and knowledge to core competencies and outsource activities in which they are less competent; can benefit from vendors' expertise. The choice of which activities to outsource is often determined by the strategic value of the activity and its level of operational performance. Generally less strategic activities that show low internal performance are more likely to be outsourced (Beaumont and Sohal, 2004).

**Variable and fractional demand:** - A small firm's limited internal resources make coping with sudden changes in demand difficult. Responses to increased demand usually lag demand as new capacity is acquired or new staff are recruited and trained. Diminished demand may necessitate dismissing loyal staff in whom training and experience has been invested. A vendor may have

ample resources. A small organization will not hire half a lawyer, but outsource its legal requirements.

### **2.6.2 Disadvantages of outsourcing**

Since outsourcing is recent tool of managers the complete costs are not yet known, which possess a risk in itself. One of the causes of outsourcing failure is lack of guiding methodology for managers and skills to manage and monitor outsourced functions (Kremic et.al, 2006). While outsourcing may seem attractive at the strategic management level, serious pitfalls are often encountered as the strategy is pushed downward into operations. At the operational level, the strategic intent tends to be lost in a hectic day to day, problem to problem business environment. Outsourcing decisions made at the operational level can easily lead to dependencies that create unforeseen strategic vulnerabilities (Ibid, 2006).

Kremic et.al (2006) listed potential risks in relation to outsourcing that are gathered from outsourcing literatures. The following are the potential risks

- Unrealized savings or hidden costs
- Less flexibility
- Poor contract or poor selection of partner
- Loss of knowledge/skills and/or corporate memory and the difficulty in reacquiring a function
- Loss of control/core competence
- Power shift to supplier
- Supplier problems (poor performance or bad relations, opportunistic behavior, not giving access to best talent or technology)
- Losing customers, opportunities, or reputation
- Uncertainty/changing environment
- Poor morale/employee issues
- Loss of synergy
- Create competitor

- Conflict of interest
- Security issues
- False sense of irresponsibility
- Legal obstacles
- Skill erosion Lafferty and Power shift to supplier

Basel committee on banking supervision paper of Outsourcing of financial services on 2005 identified and explained some of common outsourcing risks of financial services encountered.

The key risks that may arise due to outsourcing are:

- Strategic Risks - The service provider may conduct business on its behalf, which is inconsistent with the overall strategic goals of the bank.
- Reputation Risk - Poor service from the service provider, its customer interaction may not be consistent with the overall standards of the bank.
- Compliance Risk - Privacy, consumer and prudential laws may not be adequately complied with by the service provider.
- Operational Risk - Arising due to technology failure, fraud, error, inadequate financial capacity of service provider to fulfill obligations and/or provide remedies.
- Legal Risk – includes, exposure to fines, penalties or punitive damages resulting from supervisory actions, as well as private settlements due to omissions and commissions of the service provider.
- Exit Strategy Risk - This could arise from over-reliance on one firm, the loss of relevant skills in the bank itself preventing it from bringing the activity back in-house and contracts entered into wherein speedy exits would be prohibitively expensive.
- Country Risk - Due to political, social or legal climate of country where the service provider is located.
- Contractual Risk - This risk arises from inability or degree of ability of the bank to enforce the contract with the service provider.
- Concentration and Systemic Risk - Due to lack of control of the bank over a service provider, more so when overall banking industry has considerable exposure to one service provider. The failure of the service provider in providing the desired services

covered by the terms of agreement or any non compliance of any legal / regulatory requirements by the service provider can lead to reputational or financial loss for the bank which can trigger a systematic risk in the banking system (Basel Committee, 2005).

## **2.7 Theoretical framework of the study**

Perceptions of decision makers towards outsourcing is discussed by Kumar and Natarajan, pp 8, (2011) as *“positive perceptions are often equated with the advantages of outsourcing and the criticality of outsourcing for the organization; negative perceptions are equated with the risks of outsourcing and the roadblocks for implementing outsourcing decisions.”*

The risk and benefits of outsourcing have influence on the attitude of decision maker towards outsourcing (Gewald and Dibbern 2009). *“Attitude towards outsourcing is positively influenced by the perceived benefits and perceived criticality of outsourcing; and negatively influenced by the perceived risks and perceived roadblocks for implementing outsourcing”* (Kumar and Natarajan, pp 8, 2011).

A way to evaluate outsourcing risks despite the non availability of quantitative data is to use the expert judgment of Bank managers. Supported by a number of studies showing that the actual outsourcing decision is strongly influenced by the particular manager in charge of the process and is thereby an individual rather than a group decision (Kakabadse and Kakabadse 2002, cited in Kremic et.al., 2006). It becomes obvious that a manager's individual perception of outsourcing risks and benefits plays a major role as an antecedent to corporate outsourcing. Therefore, if managers are involved in the decision process towards BPO it is of utmost importance how they perceive the risks as no reliable objective measure is currently available.

The perceived risks and benefits associated with BPO strongly influence managers' intention to outsource business processes. Hence detecting the perceptions of decision makers in outsourcing is important to identify the reasons of currently outsourced activities as well as future trends of outsourcing practices.

Prasad et.al (2011) has seen various dimensions of outsourcing that have been identified from both in practice and literature as:

- 1) Shoring model (vendor location/service creation),
- 2) Sourcing model (vendor type),
- 3) Engagement model (number of vendors engaged), and
- 4) Duration of the engagement (contract periods).

The ownership of the outsourcing facility and the transfer of assets is also an important dimension of outsourcing. Dibbern and Heinzl (2001) cited in Prasad et.al (2011), for example, distinguish between the procurement of a service from a legally independent entity (third party vendor) and from profit centers with capital ties to the enterprise (e.g. subsidiary or joint venture). Another important dimension of outsourcing is the number of vendors engaged by a client (Lacity and Willcocks, 2001, cited in Prasad et.al, 2011).

An organization may choose to engage a single vendor (single outsourcing) for all its outsourcing needs or may engage multiple vendors for the same (multiple outsourcing) depending upon several factors, like nature of the activities, vendor's capabilities, client's ability to manage vendors, availability of vendors, and maturity of outsourcing market, and so on (Prasad et. al, 2011).

Gallivan and Oh (1999) cited in Prasad et.al (2011) analyzed various IT outsourcing relationships as business alliances and described client vendor relationship (single client/single vendor, multiple clients/single vendor and so on) and highlighted that these simple relationships may prove to be risky for the client due to the dependency on single vendor. Engaging with single vendor poses a serious risk of vendor dependency, especially in an immature outsourcing market, and hence, it is prudent for the organizations to consider engaging multiple vendors for outsourcing.

The scope or the extent of outsourcing is also a very important dimension of an outsourcing decision. There are terms Total or complete outsourcing and selective or partial outsourcing describing the coverage or scope of the outsourced services. In a total (complete) outsourcing arrangement, a client outsources a complete activity or a business process or an entire function, while in selective (partial) outsourcing, the client procures services from the vendors only partially (Ibid, 2011).

As the outsourcing practice was getting widely adopted across several industries and geographies, coupled with the maturing of the vendor market and the outsourcing services being offered in a variety of packages, several new sourcing models have emerged during the late 1990s (Prasad et. al, 2011). Therefore this research is anchored based on the above theoretical frameworks.

## **CHAPTER THREE**

### **METHODOLOGY**

The study investigates challenges and opportunities of outsourcing practice in Ethiopia with particular focus on the banking industry. In order to gather relevant data and draw useful and realistic conclusion, the researcher has used the following methodology for the research.

#### **3.1 Research design**

A descriptive type of research design is used for the study. The reason behind using descriptive study design is because the researcher is interested in describing the existing situation under study. The study shows the current practices of outsourcing within the banking industry. In addition, the bank managements and senior officers' perceptions toward outsourcing in terms of strategic business tool are described by gathering the relevant information and analysis. The study is cross-sectional in the sense that relevant data were collected at one point in time.

#### **3.2 Source of data**

Both primary and secondary data were used for the study. Primary data were gathered using questionnaire and semi-structured interviews, whereas secondary data were collected from reports, websites, and various unpublished and published materials through documentary analysis.

#### **3.3 Population and sample**

The population of the study is Ethiopian banks that are operating within the country. There are sixteen private and three government owned banks in Ethiopia. Among them the study gathered relevant information from five banks as a sample. In order to represent the population the sample contains two government banks and three private banks. Stratified random sampling technique was used to select the sample banks based on lottery method. Accordingly, Commercial Bank of

Ethiopia (CBE) and Development Bank of Ethiopia (DBE) from government owned banks and Awash International Bank (AIB), Abay Bank (AB), and United Bank (UB) from private banks have been selected as a sample. The study concentrates on three areas of business process. These are Human Resource Management (HRM), Information System Management (ISM), and Facility Management (FM). Various studies confirm that a worldwide trend shows these three areas of business activities widely outsourced. Data were collected from the above five banks managers experts, and senior officers. They were contacted from the three business process.

Purposive sampling technique was applied to distribute the questionnaire for respondents in each bank and in each business process. Respondents from each bank of the three business areas which are from HRM, FM and from IT business activities were contacted. Hence, the size of the sample reaches 100 respondents. The determination of the sample size based previous works in similar studies. The main purpose applying purposive sampling technique in this study is to gather information from senior management and officers who have relatively high role in decision making process in relation to outsourcing. Their perception influences their support for outsourcing decisions.

Semi structured interview is another tool used to gather data on practical activities of the banks in relation to outsourcing. Interview were made for the selected five banks outsourcing department managers or in related areas to cover more practical aspect of outsourcing and this was done based on purposive sampling methods.

Besides, secondary sources were used for supplementary purpose. Secondary sources include bank's annual report, unpublished internal reports and prior research reports.

### **3.4 Development of instrument**

The survey questionnaire has six sections. The first section was designed to collect personal information about the participants relevant to verify key informants. The second section contains measurement questions that assess the current practice of outsourcing in the bank. The third and fourth sections are designed to collect information regarding the perceptions of senior officers

and managers to outsourcing in terms of benefits and risks. The fifth section contains a rating scale measurement questions designed to collect the roadblocks of outsourcing and the last section, deals with question relating to criticality of outsourcing as a business strategy.

The questionnaire design used two scales to collect the data. The nominal scale and five point Likert scale ranging from five (very high) to one (very low) is used to measure the responses. Most of these designs have been adapted from previous survey done by Kumar and Natarajan (2011) with some modification by the researcher to fit for the Ethiopian context and this research purposes.

With regard to interview, semi structured question were prepared to address actual practices of outsourcing of banks. The question was used as initiators for discussion but during the interview. Based on the discussion necessary questions were raise in standing of interviewee response.

### **3.5 Data collection procedure**

The researcher adopted three steps in collecting the data for the study. First, relevant literature was reviewed to get adequate information on the topic. Second, objectives and research questions were formulated to show the direction of the study. Third, data gathering tools were developed. After the questionnaire was distributed and collected, interview with the senior managers and officers of the bank were conducted.

### **3.6 Method of data analysis**

Statistical Package for Social Science (SPSS) software for version 20.0 was used to compute and analyze the data. The statistical tools are used in the analysis of data include percentage, mean, standard deviation, chi square and rank. Graphs and tables are used for presentation of data.

Chi square test is applied in order to test significances of relationships among different sets of variables. Pearson Chi square test is used using SPSS (IBM Version 20). The reason for using Pearson Chi square test is because of its appropriateness to measure association among two

variables. The variables considered under this study are ordinal variables, which are perceived degree of expected benefits of outsourcing, perceived degree of expected risk related to outsourcing and the level of perceived roadblocks on outsourcing practices. Each of the three ordinal variables is checked if they have a relation with the perceived criticality of outsourcing as a business strategy, taking  $\alpha= 0.05$  at different degrees of freedom.

## **CHAPTER FOUR**

### **DATA PRESENTATION, ANALYSIS AND INTERPRETATION**

This chapter presents analyzed results and interpreted discussions of the data obtained from the primary sources as well as secondary sources. The primary data was obtained from the questionnaire and semi structured interview questions which are designed to collect the necessary data to answer the research questions. The questionnaire was administered for one hundred respondents, from the five sampled banks, situated in Addis Ababa, Ethiopia whereas interviews were made with five senior higher management officers. This chapter is organized based on data gathering tools. Hence, first all the data from questionnaire are presented and secondly data from interview and documents are analyzed.

#### **4.1 Results of data gathered from questionnaires**

This part has seven sections in relation to data of questionnaire. The first section deals with the demographic data of respondents. The second section deals with general practice of outsourcing in banks. The perceptions of senior officers and bank managers toward the benefits and risk of outsourcing are presented in third and fourth sections respectively. Fifth section deals with the obstacles to outsource business process. The last section reveals the criticality of outsourcing as a business strategy.

##### **4.1.1 Background information of respondents**

One hundred questionnaires were distributed to the respondents and out of the 100 questionnaires 78 of them were collected with a response rate of 78%. However, only 74 responses were valid with complete answers. The demographic characteristics include: designation, gender, age, level of education, and length of service. This aspect of the analysis deals with the personal data on the respondents of the questionnaires. Table 1 to table 4 below shows the details of background information of the respondents.

Table 1: Respondents category by bank ownership and position

Position		Bank		Total	
		Private	Government	Frequency	Percent
Managers		16	12	28	38
Experts /Senior Officers		18	28	46	62
Total	Frequency	34	40	74	100
	Percent	46	54	100	

The above table shows that 54 % of the respondents were from the state owned banks and 46% of them were from private banks. In terms of organizational hierarchical positions all participants were senior officers and managers who have relatively higher information and as well as experience within the banks. Among respondents 38% were managers whereas the rest of them (68%) were experts and senior officers.

Table 2: Respondents length of service on current job and their department

Respondents department/Business process		Length of service on current job				Total	
		Below Six Month old	6 month to 2 years	3 – 5 years	Above 6 Years	Frequency	Percent
Information Technology		2	2	4	4	12	16
Human Resource		1	8	21	7	37	50
Facility(property) Management		2	12	10	1	25	34
Total	Frequency	5	22	35	12	74	100
	Percent	6	30	47	16	100	

Table 2 demonstrates respondent's current job and their experience on their current job. Majority of the respondents are from HR department which cover 50% of the respondents. 34% and 16% of the respondents were from Facility or property management department and information technology department respectively.

Experience of respondent on their current job is shown that 63% of the respondents have more than three years of work experience on their current job. Thus, the survey response can be relied upon data gathered from these groups to reflect the current practice and understanding of outsourcing with in the banking sector.

Table 3: Educational level and experience of respondents

Experience	Educational Level			Total		
	College Diploma	First Degree	Second Degree & above	Frequency	Percent	
Below 1 year	2	2		4	5	
1 – 5 years	1	7	11	19	26	
6 – 10 years		22	2	24	32	
Above 10 years		24	3	27	36	
Total	Frequency	3	55	16	74	100
	Percent	4	74	22	100	

The above table presents information relating to personal attributes of the respondents in relation to education and job experience. With regard to experiences 68% of the respondents have more than five years of experience. The respondents are well educated in which 96% holding at least a first degree and all the respondents occupying senior officer and management positions. This suggests that all the respondents were well versed with the policies and operations of the bank, and have good understanding in outsourcing decisions within their organizations.

Table 4: Respondents age and sex

Respondents Sex		Respondents Age				Total	
		Below 25 years old	26 – 35 years old	36 – 55 years old	Above 55 Years old	Frequency	Percent
Male		2	32	8	1	43	58
Female			21	10		31	42
Total	Frequency	2	53	18	1	74	100
	Percent	3	72	24	1	100	

From the above table about 58% respondents are male the least amount 42% are females. The age majority of the employees are between 25 than 35 years old which comprise 72% of the respondent and 24% of them aged within 36 to 55 years. This shows respondents of the study have a good mix of sex as well as age groups.

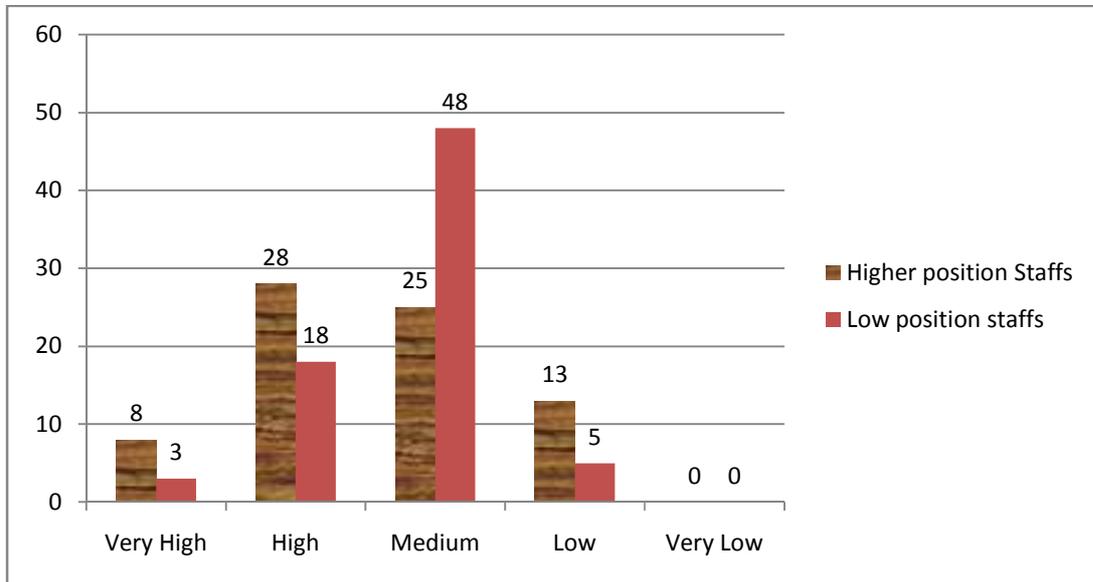
Generally from the details of background information of the respondents it is possible to conclude that respondents of the study have good experience and educational background and have a good mix of sex as well as age groups that help to have better complete perspectives of outsourcing that would be reflected on their perceptions.

#### 4.1.2 Trend and practice of outsourcing

##### 4.1.2.1 Outsourcing concept awareness level in banking sector

To assess the awareness level of bank staffs about the concept of outsourcing, respondents are asked to reflect their observations of subordinate and supervisors level of awareness in ranging from very high to very low. Result of respondents summarized in figure 2.

Figure 2: Awareness levels of bankers about outsourcing



According to figure 2, majority of the respondents believe that their subordinates as well as their supervisor have more than medium level of awareness about the concept of outsourcing. Thus, the result shows bank staffs have reasonable level of awareness about the concept of outsourcing.

Awareness among organizations staffs to a strategy is important for the strategy successful implementation. Hence the above medium level of awareness on the bank staffs will have its own positive impact on success of outsourcing strategy.

#### 4.1.2.2 Trends of outsourcing practice

Globally, according to Federal Bank of New York (1999) the financial services sector show a gradually growing trend in outsourcing, both in terms of nature and scope of activities outsourced. To assess the future trend of outsourcing practice in Ethiopian banking sector respondents are asked their perception of future potentials of outsourcing.

Figure 3: Future growth of outsourcing

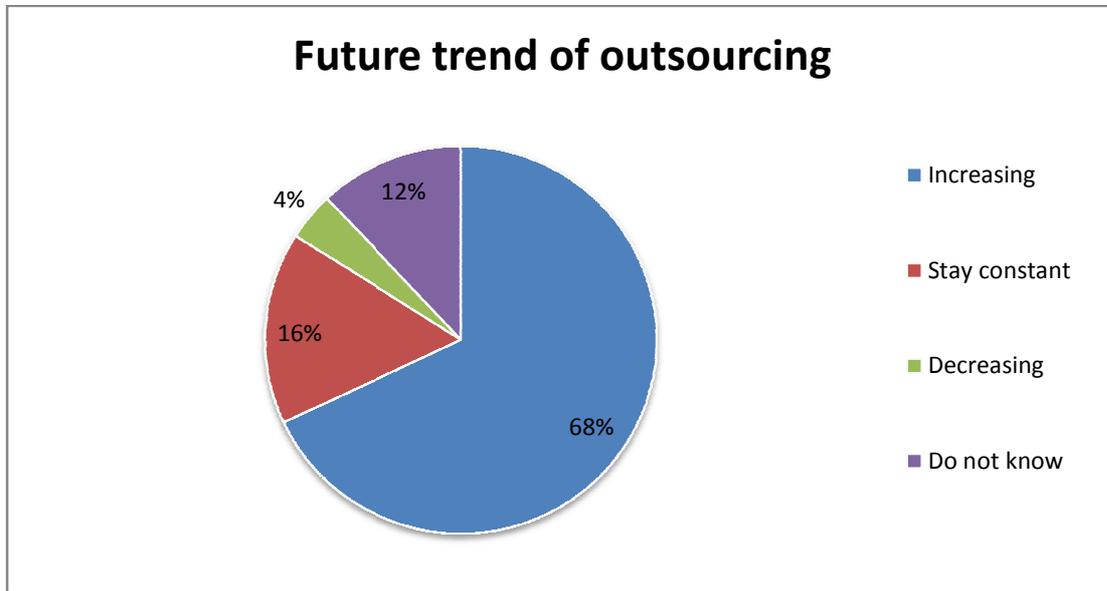


Figure 3 show that 50 respondent which is 68% of the respondents believe that outsourcing practice is increasing. The other 16% of the respondents believe that outsourcing services will not be change within the bank in the future or it will stay constant.

#### 4.1.3 Perception of bank managers and senior officers to outsourcing benefits

The perceived benefits associated with outsourcing strongly influence managers' intention to outsource business processes. Hence revealing the perceptions of decision makers and their subordinates in outsourcing is important to identify the reasons of currently outsourced activities as well as future trends of outsourcing practices. The perceptions of respondents on the degree of expectation of benefits from outsourcing were asked and measured using five-point likert scale (Scale: Very high to Very Low). Table 5 shows the result.

Table 5: Perception of bank managers and senior officers to outsourcing benefits

	N	Mean	Mode	Std. Deviation	Rank
Achieve better focus on core competencies (core business)	74	3.68	4	1.366	1
Cost shifting (from 'fixed' to 'variable')	74	3.62	3	1.003	2
Management convenience (spreading risk)	74	3.54	4	1.088	3
cost cutting	74	3.51	4	1.208	4
Improved operational efficiency	74	3.49	4	1.010	5
Improved customer service	74	3.41	3	1.134	6
Access to new and updated technologies on continuous basis	74	3.41	4	1.158	6
Access to new capabilities and skill sets.	74	3.41	4	1.271	6
Process improvement (restructuring and process standardization)	74	3.38	3	1.030	9
Improved business intelligence	74	3.30	4	1.362	10
Introduce new products/services (with quick time-to-market)	74	3.19	3	1.401	11
Overall outsourcing benefits	74	3.49	4	.798	

The results of the questionnaire responses on perceived benefits of outsourcing are shown in Table 5. The respondents are generally in agreement that outsourcing process brings benefits to a

bank. The mean value of 3.49, mode 4, and 0.798 SD, on five point likert scale for overall benefit for the organization indicates that respondents expected high level of outsourcing benefits.

The analysis further shows that the main motivation for outsourcing comes from the perception to achieve better focus on core competencies (core business), with mean value 3.64 and mode value 4 represent high degree of expectations on outsourcing benefit. Cost shifting (from 'fixed' to 'variable') mean (3.62), mode (3) and SD 1.003, and Management convenience (spreading risk) mean (3.54), mode (4) and SD 1.088 are ranked second and third next to focus on core business. Introduce new products/services and improved business intelligences are the least expected benefits of outsourcing.

Finding of Seth and Sethi, (2011) also supports this finding where managers want to engage their internal staff in strategic functions and entrust the routine and non-core functions to third party service providers. Recognizing the fact that senior management needs to get out of mundane day to day processing work and focus instead on strategic planning, core competencies, customer satisfaction and decision making, a number of large companies, across globe have begun selecting for outsourcing of their HR services.

According to Gewald and Dibbern (2005), cost advantages are the prevailing reason why corporations choose to outsource parts of their business. But their study in German banking sector shows that business value seems to be replacing cost reduction as the main motive for outsourcing.

#### **4.1.4 Perception of bank managers and senior officer for risk related to Outsourcing**

The degree of perceived risk due to outsourcing was asked to respondents on the likert scale (Scale: Very high to Very Low). The insight gained in this study is the ranking of the different risks from Ethiopian context instead of merely naming them.

Table 6: Perception of bank managers and senior officers for risk related to outsourcing

	N	Mean	Mode	Std. Deviation	Rank
Data security	74	3.46	4	1.184	1
Data confidentiality	74	3.41	4	1.158	2
Loosing process control	74	3.32	3	.995	3
Regulatory violations and legal obligations	74	3.27	4	1.138	4
Complexity in vendor relationship management	74	3.27	3	.983	4
Unable to realize expected deliverables/benefits	74	3.24	3	1.057	6
Increased management complexities	74	3.22	4	1.174	7
Over reliance on vendors	73	3.16	3	1.093	8
Overall outsourcing risks	74	3.35	4	.818	

Analysis of the section on the level of outsourcing risk indicates that the highest expected risk from outsourcing are data security and data confidentiality in the banking sector in Ethiopia with mean value of 3.46 and 3.41 respectively and mode value 4 which is above normal degree of outsourcing risk expectations. The perception of high degree of outsourcing risk of data-related risks (Data security, Data confidentiality) may be explained by the seriousness the banks attach to the principle of confidentiality and the sensitivity of banks customer data.

Over reliance on vendors and increased management complexities are the least degree of risk attached to them. Possible reason for the least degree of risk attached to Management and policy-related risks (Losing process control, Regulatory violations and legal obligations, Complexity in vendor relationship management, Over reliance on vendors, Increased management complexities, Unable to realize expected deliverables/benefits) may be believes of banks internal capacity to manage and to substitute outsourced services easily.

#### 4.1.5 Major Roadblocks of outsourcing

To implement outsourcing as a strategy there are challenges from various points. These challenges impact vary from country to country from sector to sector. Degree of impact of major Roadblocks for Bank to outsource were asked and measured using likert Scale (Very high – 1, High – 2, Neutral – 3, Low – 4, Very Low – 5).

Table 7: Outsourcing obstacles Level of impact

	N	Mean	Mode	Std. Deviation	Rank
Absence of matured vendor market	74	2.24	1	1.373	1
Size and scale of the operations/organization	74	2.35	1	1.349	2
Infrastructure inadequacy	74	2.38	2	1.392	3
Regulatory and policy restrictions	74	2.54	2	1.295	4
Resistance from Employee union	74	2.73	3	1.436	5
Overall roadblocks of outsourcing	74	2.46	2	1.113	

Table 7 shows that 'Absence of matured vendor market' is the highest roadblock to outsource with 2.24 mean values that nearly equal to high degree of impact it has on outsourcing. Size and scale of the operations/organization the second most challenger for outsourcing with the mean value of 2.27. In the same way Resistance from Employee union is the least barrier for outsourcing with the mean value 2.70 and Regulatory and policy restrictions is also less barrier with the mean value of 2.51.

This finding strengthens the finding of (Kumar and Natarajan, 2011 cited in Adeleye et al., 2004) outsourcing among Nigerian banks that the non-availability of a matured vendor market can be a big roadblock which not only impedes the outsourcing activities but also contributes to the vendor-related risks of outsourcing.

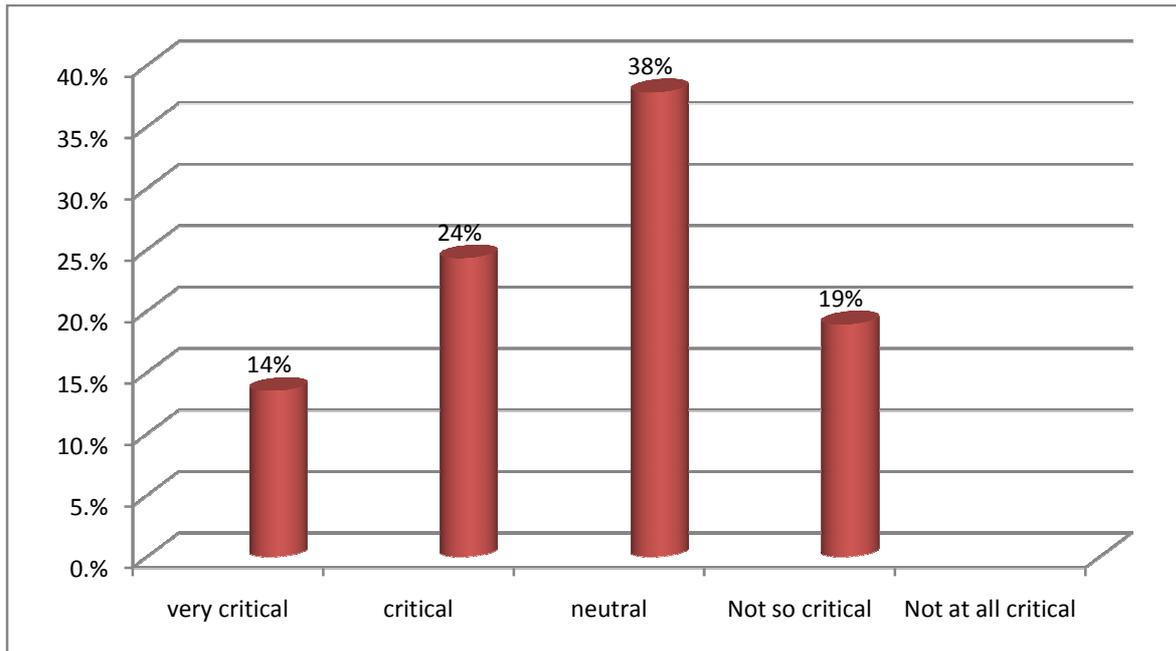
According to Kumar and Natarajan, (2011) Reserve Bank of India developed initiatives to provide a stable and reliable framework for banks to adopt outsourcing practices. But the restrictions imposed by these regulations were stringent enough to call for concerted efforts to remain compliant on the part of both the banks as well as the outsourcing service providers; thus posing a serious roadblock to engage in outsourcing activities. In highly unionized employee resistance from employee unions can also be a serious impediment to outsourcing (Kumar and Natarajan, 2011).

Based on the above discussion it is possible to infer that lack of matured vendor market is major obstacle for outsourcing in Ethiopia.

#### **4.1.6 Criticality of outsourcing as a business strategy**

The perceptions of experts, senior officers and managers regarding the criticality of outsourcing as a business strategy presented in figure 4. The figure shows that 38% of the respondents believe that outsourcing is a critical business strategy for their banks. In the same way 38% of respondents expressed outsourcing as basic strategy for banks and still 19% of them consider outsourcing as it is not so critical. Outsourcing is a critical aspect of financial institutions to survive in today's business environment (Federal Bank of New York 1999).

Figure 4: Criticality of outsourcing as a business strategy



#### 4.1.7 Chi square test

The relationship among expected benefits of outsourcing, perceived risk of outsourcing and perceived roadblocks with criticality of outsourcing as business strategy of variables is tested.

##### 4.1.7.1 Expected benefits of outsourcing Vs criticality of outsourcing as business strategy

The result for the test for independence between perceived benefits of outsourcing and the perceived criticality of outsourcing as a business strategy obtained from the SPSS experimentation is shown below.

Table 8: Chi square test result of Perceived benefits of outsourcing Vs criticality of outsourcing as business strategy

		Criticality of outsourcing as a business strategy				Total
		Not so critical	Neutral	critical	Very critical	
Outsourcing benefits	Low	6	2	0	0	8
	Neutral	0	10	16	2	28
	High	4	8	10	10	32
	Very high	0	2	2	2	6
Total		10	22	28	14	74

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	40.645	9	.000
Likelihood Ratio	37.868	9	.000
Linear-by-Linear Association	11.224	1	.001
N of Valid Cases	74		

As the calculated Chi square result, 40.645 is greater than the critical value (tabulated Chi square value at  $\alpha= 0.05$  with 9 degrees of freedom (16.919), we reject the null hypothesis. Therefore, it is possible to conclude that there is a relationship between benefits of outsourcing and criticality of outsourcing as business strategy.

#### 4.1.7.2 Perceived outsourcing risks Vs Criticality of outsourcing as a business strategy

The result for the test for independence between the level of expected risks from outsourcing and the perceived criticality of outsourcing as a business strategy obtained from the SPSS experimentation is shown on table 9.

Table 9: Chi square test result of perceived outsourcing risks Vs criticality of outsourcing as a business strategy

		Criticality of outsourcing as a business strategy				Total
		Not so critical	Neutral	critical	Very critical	
Outsourcing risks	Very low	0	2	0	0	2
	Low	2	2	2	2	8
	Neutral	4	10	12	2	28
	High	2	8	14	10	34
	Very high	2	0	0	0	2
Total		10	22	28	14	74

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	25.446	12	.013
Likelihood Ratio	21.412	12	.045
Linear-by-Linear Association	1.403	1	.236
N of Valid Cases	74		

As the calculated Chi square result, 25.446 is greater than the critical value (tabulated Chi square value at  $\alpha= 0.05$  with 12 degrees of freedom (21.026), we reject the null hypothesis. Therefore, we conclude that there is a relationship between the level of perceived outsourcing risk and criticality of outsourcing as a business strategy.

#### 4.1.7.3 Roadblocks of outsourcing Vs Criticality of outsourcing as a business strategy

The result for the test for independence between perceived roadblocks of outsourcing and the perceived Criticality of outsourcing as a business strategy obtained from the SPSS experimentation is shown below.

Table 10: Chi square test result of perceived roadblocks of outsourcing Vs criticality of outsourcing as a business strategy

		Criticality of outsourcing as a business strategy				Total
		Not so critical	Neutral	critical	Very critical	
Roadblocks of outsourcing	Not applicable	0	0	2	2	4
	Very low	2	2	0	2	6
	Low	2	14	10	4	30
	Neutral	4	4	12	4	24
	High	0	2	4	0	6
	Very high	2	0	0	2	4
Total		10	22	28	14	74

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	27.752	15	.023
Likelihood Ratio	32.634	15	.005
Linear-by-Linear Association	.326	1	.568
N of Valid Cases	74		

The calculated Chi square result, 27.752 is greater than the critical value (tabulated Chi square value at  $\alpha= 0.05$  with 15 degrees of freedom (24.996), resulting to reject the null hypothesis. Therefore, we conclude that there is a relationship between the level of the management support (while works identify problems and give solution) and the perceived organizational success.

## **4.2 Findings from interview and its discussions**

Interviews were made with four bank senior managers from each sampled banks, in order to gather practical activities of outsourcing. From government banks property management business process manager and corporate human resource development directorate director were interviewed. From private banks human resource manager, procurement and facility management directorate director and general service manager were interviewed. Semi structured interview questions were prepared to gather more information from the respondent's feedback. For the purpose of presentation related questions and their responses are presented together in the following manner.

### **1. When did you start outsourcing? What are outsourced services of the bank? What activities are planned to be outsourced in the near future?**

The experiences of outsourcing vary from bank to bank. According to interviewees response outsourcing started within the range of seven to three years ago on their banks. CBE was started outsourcing before seven years ago and DBE also started outsourcing five years back. But AB and UB started outsourcing three and two years ago respectively. Far from the others AIB did not outsource any of commonly outsourced service for external service providers with the exception of vehicle maintenance. Generally government owned banks are relatively started outsourcing early than private banks. This variation may be due to their establishment period; government banks are older than the private banks. Therefore outsourcing practice in banking sector in Ethiopia is almost new as it is compared to global financial sector trends.

The four sampled banks with the exception of AIB started outsourcing with non clerical services; specifically with security services. AIB outsource vehicle maintenance. The other service areas mostly outsourced by banks currently are cleaning services, supply of labor for messenger services and other temporary support works. Information technology services are not considered by the respondents as a real outsourcing deal rather they consider it as one time purchase. But one respondent mention that implementation of core banking software was outsourced partially for Indian firm for three years of contractual agreements to provide technical assistance, however

internal staffs were administering the whole process of implementations. Outsourcing of non core business is varying among banks.

Respondents mention that Transportation service, Maintenance and servicing of car service, Procurement activities, performance management, medical service, ATM, Card banking, external recruitment, mail service, and drivers are planned to be outsourced.

In contrary to the above discussion one of the respondents said that currently there is no plan to outsource other activities of the bank, rather due to management difficulty of vender relationships they are considering turning back what they outsourced which is security services. As the interviewee disclosed cleaning and messengers are outsourced in other banks but the bank believes that outsourcing these services are too risky, since the documents exchanged between offices are confidential as well as almost they are money.

Documents on bidding found at CBE reveal that, invitation for expression of interest on potential outsourcing services show fifteen services that were selected for outsourcing. This includes Cleaning Service, Audio Visual Service, External Recruitment & Selection Service, Building Administration and Maintenance Service, Promotional Service etc. See appendix.

In relation to the service provider location, all venders are local companies that supplies non clerical services like security, maintenance and cleaning services with exception of information technology services provided by foreign company. In relation to number of vendors engaged by banks; currently banks hire one vender for one service type and they engaged in contracts with various venders for different services. This shows that at least more than two venders are being managed by each bank. Duration of the engagement is varying from contact to contract and from bank to bank experience, but generally contract periods set between one to two years.

Another important dimension of outsourcing is the ownership of service providers engaged in contracts. This is whether or not service provider has financial and other stakes with the outsourcing company. Based on this dimensions CBE works with its own subsidiary company. Private Banks are engaged in the procurement of a service from a legally independent entity

(third party vendor). Interviewee responses regarding outsourced service are summarized in to tables 11.

Table 11: Summarized current status of outsourcing services

Function	Already Outsourced	Under consideration	Not considered For outsourcing	Reintegrate Functions
Human Resource Functions	1	3	1	
Promotion and Marketing functions	1	1	3	
Information Technology functions	1	1	3	
Maintenance services	2	3		
Security services	4		1	
Cleaning /Janitorial services	3		1	
Transportation services		4	1	
Procurement and logistics services		3	2	

Table 11 shows the level of currently outsourcing for each function. The level of outsourcing was captured using for constructs, dependent upon whether the bank; already outsource the function, is under consideration, has decided against or reintegrate a particular function with others.

Analysis of the section on the level of outsourcing indicates that security function and janitorial functions are the most outsourced in the banking sector in Ethiopia all interviewees indicating

that their banks have already outsourced the functions. The high rate of outsourcing of these functions may be explained by the emergence of private companies offering the services.

According to Barako and Gatere (2008) ATM services and card processing are the most outsourced function in Kenyans banking sector. Literature on outsourcing states a significant portion of activities that are outsourced globally by different organizations across different industries in different countries, are horizontal business activities, e.g., customer care, payroll, recruitment, training and development, etc. (Prasad et. al, 2011).

Whereas according to Kumar and Natarajan (2011) the outsourcing practices of Indian banks shows that they have serious reservations in outsourcing their horizontal business activities. They preferred not to outsource their customer care and technical help desk activities, Sales and marketing activities, activities that involve direct dealing/interaction with the customer (e.g., sales, marketing, customer care etc.).

From the above discussion it is possible to infer that the level of outsourcing in Ethiopian banks is at its infant stage in terms of type of outsourced services which limited to non clerical services (security services, cleaning service, information technology services, and supply of temporary labor services). However future growth seems to be expanding towards basically supporting activities that are common across industries independent of the nature of the business of an organization.

Banks do not consider software purchasing and implementation as outsourcing, information technology services are outsourced partially for foreign and local companies for its implementation and technical supports. Outsourcing is more common in information technology for services that have usually been regarded as intrinsic to managing a business. In some cases, the entire information management of a company is outsourced, including planning and business analysis as well as the installation, management and servicing of the network and workstations (Gewald et. al, 2006).

## **2. What was the motive to outsource?**

In relation to driving force to outsource interviewed participants mentioned management convenience, focusing on core business, and cost saving as a motivational factor for outsourcing.

Management convenience; the main motive for outsourcing those non clerical services are administrative issue. Management of non core functions and administering non clerical staffs are highly difficult. There was high absenteeism with the reason of sick leaves, they don't arrive on time on their jobs, managing their benefits' was very routine in relation to their uniforms, insurance, medical and the like. Management of non clerical benefits, government regulations, programs and follow up of their performance are routine and takes more time of managers. As one interviewee said on average seven security guards are hired for a single branch. The process of hiring and administering is quite difficult as compared to clerical staffs considering their level of contribution for bank competency and lack of qualified professionals. Other issue raised is that in our country there is lack of proper certification and professionalism in non clerical services like cleaning, security guards and massagers. Handling and managing these personnel are difficult for bank managers. Outsourcing is a good ways of handling these services by external expertise.

Focusing on core function is the other main driving force for outsourcing in banking sector of Ethiopia. The other major motive of the bank to outsource is to focus on core business. Interviewee from CBE said that the bank has a vision to be a world class commercial bank by year 2025. In order to realize its vision the management as well as its staffs should focus on strategically important core areas of the bank. Outsourcing noncore activities to external service providers who has a competency and economic scale advantage is a critical strategy of the bank. The other respondent discussed that the bank is new and it wants to be internationally competent bank. To be nationally and internationally competent bank, global thinking is important and one of the currently applied strategies of management is outsourcing. The respondent's views are supported by Kim and Won (2007) conclusions that by outsourcing noncore activities for vender organizations, clients can focus on their core activities that give them competitive advantage and improve overall performance.

Based on interviewees response cutting cost was not the main driver for outsourcing. However cost saving is considered for decision to outsource a business activity. Some of mentioned costs saved from outsourcing are Insurance, medical, training and development, uniform, and the like cost for non clerical staffs. Interviewee from AB discussed that internally there was a high demand for outsourcing since the bank is new it has no own facilities. Most of the offices are rented and there is a problem of facility in general. Hence cost cutting is one of the major drivers for outsourcing.

From the above discussion it is possible to infer that management convenience, and focus on core activities are major reasons for outsourcing. However cost cutting is also reason for outsourcing, yet it is not the major motive for outsourcing. There is no difference between government banks and private banks in terms of outsourcing drivers. This varies from the conclusion of (Kakabadse and Kakabadse, 2000a, cited in Kremic et. al., 2006) that Cost and strategy motivations commonly drive outsourcing by private organizations and political agendas often drive outsourcing by public organizations.

Generally from both results of questionnaire and interview, unlike other studies, this research found that cost reductions are not the key driver for outsourcing, but the ability to focus on core competencies and management convenience are the main factor for outsourcing. Increased cost transparency which is cost shifting from fixed to variable also turns out to be more important than pure cost reduction. Overall, this finding is similar with findings of Gewalt and Dibbern 2005; study on German Banking Industry, over the Influential Role of Perceived Risks versus Perceived Benefits in the Acceptance of Business Process Outsourcing. German banks can be seen to favor business value over cost reductions in business process outsourcing engagements.

### **3. What was the process of outsourcing?**

The response of interviewees on their bank experience regarding the process of outsourcing is more or less similar. In terms of handling outsourcing contracts CBE is relatively more organized and a separate outsourcing management offices are established. Other banks facility and property management business unit or general service unit handles the administration and

follow-up of the outsourcing contracts for currently outsourced services which are security and cleaning services. Decision to outsource an activity is done by Top management of banks.

The first step for outsourcing is identification of potential business activities for outsourcing. According to interviewee the basic evaluation criteria used were whether the service is core business of the bank or not and the competency level of the bank. Mandate of the bank and strategic importance of the business are the basic factors for weight the business as Core business of the bank. Level of competency of the bank over each service are also based on various factors such as the internally available and required material and human resource, Cost Savings, Improve service level, Reduce risk, Control of budget, Lower ongoing investment, requirement in internal infrastructure, Increase flexibility to meet changing business conditions, Acquire innovative ideas. Generally less strategic activities that show low internal performance are more likely to be outsourced (Beaumont and Sohal, 2004).

Based on the assessment potential outsourcing services selected then using bidding process service provider was selected. Secondary analysis of documents show that CBE was invited for expression of interest bid for those potential outsourcing services identified as potential outsourcing business activities. Bidding document on outsourcing services of CBE shows fifteen services that were selected for outsourcing see appendix.

Bidding selection criteria (evaluation measurement) were as follows 30% financial aspects; price for the service and 70% technical aspects which includes; management experience; past performance of reference; organizational structure; human resource organization; proportional salary payment for outsourced staffs.

From the above discussion of interviewee's responses and documents analysis we can deduce that outsourcing decisions were made by top managements. Assessment of potential activities based on the competency and core activities are seen from banks. Outsourcing like any other purchasing process bidding procedure is applied to select the right service provider.

To sustain the positive benefits that it brings to the organization, it is important to have a well managed plan of action for the outsourcing process. This includes deciding which activities or tasks to outsource, which companies should be hired to perform these tasks, how to manage the outsourced business process, how to agree on payment terms, and how to ensure that the desired results are achieved (Beaumont and Sohal, 2004).

For question raised, what was any firing of staffs due to outsourcing, Interviewees disclosed that no single individual is fired. Due to natural process, the number of staffs in those areas of service to be outsourced decreased. Some of them were retired, others who upgrade themselves promoted and others are dead and the size of non clerical staffs decreased. In the mean time contractual bid was made and a service provider was selected to fill the gap. Partial outsourcing was applied and through time as internal staffs decrease the service provider supplies the required amount of labour and fills the gap.

#### **4. Is there any challenge to outsource from the market?**

Currently banks outsourced some of non clerical services that have relatively good supply and ability from the market. These activities are Janitor service and security guard service. These services are currently provided by the market with some level of competency. There are challenges from the market. In most of the services, there is lack of well qualified service provider. Example mentioned by interviewee that transportation service was planned to be outsourced but from the market assessment there are some venders that render the service but their services are not guaranteed in terms of quality. So the bank decided to postpone outsourcing of transportation. In relation to cleaning, messenger, security service there are considerable number of venders with different capacity and experiences.

Based on what the banks outsource specifically to security and cleaning service there are a number of challenges. During bidding time there were a number of service providers and they presented their capacity and win the contract. But after contractual agreement is signed their focus will be money only. They are not professionals, they are not organized and they don't have proper controlling system. Their HR is not strong, and even there is nepotism within the

organizations. In order to maximize the profit, service providers have contracted with many companies beyond their capacity as a result they offer service which does not meet their customers' expectation.

Lack of ownership and belongingness is the major challenge faced by banks from the outsourced staffs. Service providers focus on money making. Hence, they pay less salary for their staffs and due to this and other management problems there is high turnover. In addition, in order to fill their financial needs outsourced staffs work more time in various organizations beyond acceptable working hours and they get tiered to give the required service efficiently.

One interviewee mentions that currently one service providers are giving security services in branch of the bank at Addis Ababa and Mekele only. On the other regions of the country the staff performs the activity. The main reasons are first they are very expensive to give service out of Addis Ababa. Secondly they are required to have license from the region to give this service on those specific areas.

Interviewee from CBE said that out of fifteen potentially outsourcing activities that CBE invited for bidding none of the services have qualified and competent service provider were presented as to the level of competency the bank expected. The market is very weak to provide quality service with required capabilities. Due to this CBE currently engaged in contract with its own subsidiary company CN so that it can support the company to get the required level of services.

Accordingly interviewee from AIB disclosed that the main reasons not to outsource what commonly outsourced services by other banks like cleaning and security services are lack of qualified service providers from the market. Study was conducted by General services department together with system reengineering division on the experience of other banks and the market. Based on the assessment it is concluded that currently challenge and risk of outsourcing outweighs the benefit hence in sourcing is the better approached. If there is professional service provider with strong capacity in terms of financial technical and human resources, the bank will outsource some of non clerical services. This idea was also expressed by other interviewees.

**5. What benefits bank gets from outsourcing? Are you satisfied with performances of service provider?**

According to the interviewee's response managers and internal staff free time for more strategic activities, cost saving, and external expertise management are the major benefits gained from outsourcing.

Banks achieved the expected benefits of outsourcing in two aspects. The first one is the administration burden of managing non clerical staffs are decreasing as compared to the previous times. Now, in outsourcing, bank is required to give payments for the service provide as per the contract and service delivery. Hence management time are free for more critical jobs than before even though managing outsourcing contract by itself has some challenges.

The second benefit the bank realized is cost reduction. Hiring, training, insurance, bonus, medical, overtime, uniform, education fees and annual leaves are costs that are reduced due to outsourcing.

In terms of service quality they are more of professionals and the company substitute inefficient, absent employees easily.

Satisfaction level of respondents of outsourcing service varies. Some of them are satisfied by comparing the challenge of internal staff management and service quality. Others are not satisfied; mentioning that vendors are not delivering what is expected by their banks. Therefore the variation in the satisfaction level of respondents regarding the outsourced services may be due to either the variation of service level provided by different service providers or the variation of expectation level of the banks.

**6. What actions does the bank take to overcome risk and challenges of outsourcing?**

To build the trust and belongingness of service provider's staffs and management the banks invites them in ceremonial events like annual bank day and special events. The banks also

provide training on the bank vision missions and also customer handling to vendor staffs. Even some of the equipments are provided by the banks to support the capacity of contracted companies and smoothing of the services.

Specific to security services issues; there is continuous meeting of banks with bank association. Through these meetings it is proposed that security service provider will be graded based on their capacity and performance from government and the banks are suggested to hire grade one security service providers.

Interviewee from private bank indicates that even if the bank does not organize separate section of outsourcing like CBE, facility management business process is responsible for the follow-up and control of outsourced service performance. Policy and procedures are being developed; proper specialized staffs are being hired to follow specific outsourced service for example chief security officer for security services.

Respondent from the CBE states that the first outsourcing periods there were private service providing companies that provides on security and cleaning services. In order to minimize risks and related challenges from the market, the bank is now working with commercial nominees, which is a subsidiary company of the bank. CN is now providing security, cleaning, messenger and temporary non clerical man power services. The bank also established and organized on section office “outsourcing management office” that administer outsourcing contracts and manages related activities. In order to follow up the quality of service provided, the bank assigned its own security manager that control the overall security level of the bank that makes sudden check-up the attendance of the outsourced staffs.

## CHAPTER FIVE

### SUMMARY OF FINDING, CONCLUSIONS & RECOMMENDATIONS

This chapter is divided in to three sections. The first section presents the summary of findings, second section is conclusion of the research and the last section suggests important points for future researches.

#### 5.1 Summary of findings

The general objective of the study is to find out challenges and opportunities of outsourcing practices in banking industry of Ethiopia. The study tries to shows the current practices of outsourcing within the banking industry by assessing the trends; identification of which activities of the banks are outsourced; the perceptions of bank management toward benefits and risks of outsourcing, the significance of outsourcing as a business strategy; and the major obstacles to outsource. In order to address these issues a descriptive type of research methodology is used. Both questionnaire and interview were applied to gather primary data. Documentary analysis also made from secondary data. Using SPSS software descriptive statistics such as percentage, mean, standard deviation and rank are applied on the analysis.

According to the discussion and analysis of the data presented in chapter four, the findings of research shows:

1. Majority of the respondents believe that their subordinates as well as their supervisors have more than medium level of awareness about the concept of outsourcing.
2. Majority of respondents 68% believe that there is an increasing practice of outsourcing. However considerable amount of study participants do not see the future potential of outsourcing practice.
3. The mean value of 3.49 on five point likert scale represent high degree of outsourcing benefit expectation in 0.798 SD for overall benefit for the organization indicates that

respondents do consider the benefits from outsourcing as significant. Achieve better focus on core competencies (core business), Cost shifting (from 'fixed' to 'variable') and Management convenience (spreading risk) are expected benefits of outsourcing ranked first, second, and third with the mean value of 3.68, 3.62, 3.54 and standard deviation 1.366, 1.003 and 1.088 respectively. Introduce new products/services and improved business intelligences are the least expected benefits of outsourcing.

4. Management convenience, and focus on core business are the main motives of outsourcing. Cost saving also considered for outsourcing decisions but it is not the major driver for outsourcing. There is no difference between government banks and private banks in terms of outsourcing motivation.
5. The highest expected risks from outsourcing are data security and data confidentiality in the banking sector in Ethiopia ranked first and second respectively. In contrary over reliance on vendors and increased management complexities are the least degree of expected risk due to outsourcing.
6. Absence of matured vendor market is the highest roadblock to outsource nearly equal to high degree of impact it has on outsourcing. Size and scale of the operations/organization the second most challenger for outsourcing. In the same way Resistance from Employee union is the least barrier for outsourcing and regulatory and policy restrictions are also fewer barriers to outsource.
7. The perception of experts, senior officer and managers regarding the criticality of outsourcing as a business strategy shows that 38% of the respondents believe that outsourcing is a critical business strategy for their banks however considerable number of respondents does not see outsourcing as a critical strategy.

8. Null hypothesis proposed on the study are rejected hence, Perceived outsourcing benefit, perceived outsourcing risk and perceived roadblocks of outsourcing have a relationship with perceived criticality of outsourcing as a business strategy.
9. Outsourcing practice in banking sector in Ethiopia is almost new as compared to global financial sector outsourcing trends. Outsourcing practice started with in seven to three years that vary from bank to bank but state banks started earlier than private banks. Level of outsourcing practice varies among banks.
10. Currently outsourced service are limited to non clerical services which are security service, cleaning services, supply of temporary labours for messengers and vehicle maintenances.
11. Other horizontal activities like transportation service, maintenance and servicing of car service, procurement activities, performance management, medical service, ATM, Card banking, external recruitment, mail service, and the like are planned to be outsourced in the future.
12. Generally banks are considering outsourcing as one of a strategic issue that decision are being made at the top management positions. Assessment of potential activities based on the competency and core activities are seen from banks. Outsourcing like any other purchasing process bidding procedure is applied to select the right service provider.
13. Managers and staffs free time for more strategic activities, cost saving, and external expertise management are the major benefits gained from currently outsourced services.
14. There are challenges from the market. In most of the services, there is lack of well qualified service provider. In relation to cleaning, messenger, security services there are considerable number of venders with different capacity and experiences. But after contractual agreement is done their focus is profit making only. Respondent disclosed that they are not professionals, they are not organized and they don't have proper

controlling system. And the other major challenge is lack of ownership and belongingness from the outsourced staffs. Service providers focus on money making hence they pay less salary for their staffs and due to this and other management problems there is high turnover on vendor's staffs.

## **5.2 Conclusion**

The main purpose of the study is to find out challenges and opportunities of outsourcing practices in banking industry of Ethiopia.

Outsourcing is a modern management technique, despite the reasonable level of awareness of bank staffs about the concept of outsourcing, level of outsourcing is at its infant stage in terms of type of outsourced services which is limited to non clerical services (security services, cleaning service, information technology services, and supply of temporary labor services). The findings also confirm that banks are willing to outsource non-core business functions, other than currently outsourced business activities. But lack qualified service provider from the market is a big barrier to outsource. Generally banks are considering outsourcing as one of a strategic issue that decision are being made at the top management positions.

The main motivational factors for outsourcing are management convenience, and focus on core business. Cost saving which is the major motive of outsourcing globally is not a major motivator for Ethiopian banks. Expected benefits of outsourcing are significant among experts, senior officer and managers of bank. Achieve better focus on core competencies (core business), Cost shifting (from 'fixed' to 'variable') and Management convenience are highly expected among other benefits. In relation to expected outsourcing risks; data security and data confidentiality are highly expected that show lack of confidence on the professionalism of service providers. There is variation in believe that outsourcing is a critical business strategy for their banks. Most of respondents expressed outsourcing as critical strategy for banks and others consider outsourcing as it is not so critical.

Finally, there are challenges from the market. In most of the services, there is lack of well qualified service provider. In relation to cleaning, messenger, security services there are considerable number of venders with different capacity and experiences. But Satisfaction level of respondents regarding outsourcing services varies. Some of them are satisfied by comparing the challenge of internal staff management and service quality. Others are not satisfied; mentioning

that vendors are not delivering what is expected by their banks. And the other major challenge is lack of ownership and belongingness from the outsourced staffs.

### **5.3 Recommendations**

Based on the analysis of results received from the questionnaire and also based on the interview with the managers of sampled banks, the researcher would like to recommend the following points

For banks and managers responsible for the implementation and management of outsourcing:

1. Focusing on the analysis and management of risks connected with outsourcing is vital for the success of outsourcing strategy. An insufficient risk analysis can lead to the choice of a bad partner, to outsourcing of the inadequate activity and to exposing the company to some unnecessary threats. Risk scenarios allow the company to prepare for the uncertain future.
2. Some of banks do not deal properly with the management of the outsourced activity. The outsourced activity should be monitored and managed. The company should have a complex overview about the outsourced activity and the control over it. Implementation of outsourcing is better realized with supervision and monitoring of outsourcing contracts. Hence to it is better to organize a separate offices rather than attaching responsibility to existing structure.
3. Indicators for assessment of the outsourcing efficiency are not being used very often. Researcher recommends the implementation of indicators directly into the outsourcing contract. Both the provider and customer should be involved in the efficiency monitoring. Monitoring of the outsourcing efficiency is crucial for a successful outsourcing project. Without such data, the bank is not able to assess the costs increase/decrease after outsourcing.

For service providers how engage in outsourcing contracts

4. Clients are becoming increasingly cautious regarding cost advantages. Therefore, outsourcing offers should emphasize growth of business value not cost reductions. Clients

tend to value quality factors like professionalism and meeting expected deliverables higher than pure cost savings.

5. Taking the perceived risks finding into account, the major expected risk of outsourcing is data security and data confidentiality; this implies lack of trust and positive attitude to the service provider. Hence it is important that service providers should focus on this area to win trust of their client. This could seem to be the key to gaining market share. This offers service providers new ideas for the development of outsourcing proposals.

For financial supervisory bodies

6. For the financial supervisory bodies; they should aware of the potential of growth of outsourcing in banking sector in Ethiopia and prepare legal directives regarding outsourcing like other countries do ahead of time.

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# **APPENDIXES**

**St. Mary University College**  
**School of Graduates studies**

Dear participants,

This questionnaire is prepared to collect data used for thesis entitled “*challenges and opportunities of outsourcing practice in the banking sector of Ethiopia*” in partial fulfillment of requirement for Masters of Arts Degree in Business Administration.

The information you provide is highly valuable to identify general practices, benefits, risks and challenges related to outsourcing. I would like to assure you that the information you provide will be used for research purpose only and all responses will be treated in strict confidentiality.

**The researcher wants to forward his deepest gratitude for your keen cooperation.**

- You are kindly requested to put “X” mark in the box that represents your opinion and the right information.

**Definition:** - Outsourcing can be defined as ‘*using an outside organization to carry out activities previously carried out within the company*’.

**Section I: Personal Data**

1.1 Ownership of your bank:  Government  Private

1.2 Designation: \_\_\_\_\_

1.3 Your department : \_\_\_\_\_

1.4 Length of Service: On current Job \_\_\_\_\_ total \_\_\_\_\_

1.5 Highest Educational Qualification: \_\_\_\_\_

1.6 Age: \_\_\_\_\_

1.7 Sex:  Male  Female

**Section II: General information on Outsourcing**

2.1 What is the level of awareness about the concept of outsourcing on your subordinates?

Very high  High  Medium  Low  Very low

2.2 What is the level of awareness about the concept of outsourcing on your supervisor?

Very high  High  Medium  Low  Very low

2.3 In the future do you believe the number of activities you outsource will?

Increase  Stay Constant  Decrease  Don't Know

**Section III:** Please indicate the 'degree of expectation' of *benefits* from outsourcing on a five-point scale. (Please put [X] in the appropriate cell against each question) Scale: **Very high – 5, High – 4, Neutral – 3, Low – 2, Very Low – 1.**

S. No.	Benefits of outsourcing	Degree of Expectation					N.A
		5	4	3	2	1	
1	Cost cutting						
2	Improved operational efficiency						
3	Improved customer service						
4	Achieve better focus on core competencies (core business)						
5	Cost shifting (from 'fixed' to 'variable')						
6	Access to new and updated technologies on continuous basis						
7	Access to new capabilities and skill sets.						
8	Process improvement (restructuring and process standardization)						
9	Introduce new products/services (with quick time-to-market)						
10	Management convenience (spreading risk)						
11	Improved business intelligence						
12	Any other, please specify						

N. A. – Not Applicable

**Section IV:** Please indicate the 'degree of perceived risk' of the following risk elements due to outsourcing. Scale: **Very high – 5, High – 4, Neutral – 3, Low – 2, Very Low – 1.**

S. No.	Elements of Risk	Degree of Expectation and /or experienced risk					N.A.
		5	4	3	2	1	
1	Data security						
2	Data confidentiality						
3	Loosing process control						
4	Regulatory violations and legal obligations						
5	Complexity in vendor relationship management						
6	Over reliance on vendors						
7	Increased management complexities						
8	Unable to realize expected deliverables/benefits						
9	Any other, please specify						

N. A. – Not Applicable

**Section V:** Please indicate the Major Roadblocks for your Bank to outsource, and the ‘degree of impact’ they have on the management decision to outsource. Scale: **Very high – 1, High – 2, Neutral – 3, Low – 4, Very Low – 5.**

S. No.	Degree of Roadblocks Impact to outsource			1	2	3	4	5	N.A.
		Yes	No						
1	Infrastructure inadequacy								
2	Regulatory and policy restrictions								
3	Resistance from Employee union								
4	Size and scale of the operations/organization								
5	Absence of matured vendor market								
6	Any other please specify								

N. A. – Not Applicable

**Section VI:** Please indicate the ‘degree of criticality’ for adopting outsourcing as a business practice for your organization. (Please put [X] in the appropriate cell against each question)

Very Critical	Critical	Neutral	Not so critical	Not at all critical

Any other comments/suggestions

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*Thank you,*

## **Semi structured Interview questions**

### **St. Mary University College School of Graduates studies**

This semi structured interview question is prepared to collect data used for thesis entitled “*challenges and opportunities of outsourcing practice in the banking sector of Ethiopia*” in partial fulfillment of requirement for Masters of Arts Degree in Business Administration. The information you provide is highly valuable to identify general practices, benefits, risks and challenges related to outsourcing.

1. What are outsourcing contracts your organization has awarded in the last 5 years? Please specify the activity outsourced, and how many year of contract agreement is signed?
2. When did you start outsourcing? What is the bank motivation for outsourcing? How is the process of outsourcing?
3. How is one business activity proposed for outsourcing? Who made the decisions? How much participation of concerned staffs considered? What is the labour union reaction?
4. What difficulty faced to outsource externally as well as internally?
5. In what bases service provider are selected? Are the service providers foreign or local company?
6. What benefits your organization realizes due to outsourcing? What risk faced/potential risks?
7. How is the relationship of the service provider in terms of contractual agreements? Are service providers performing to the require standards? Who follow their performance?
8. How is the level of interaction and integration between the service provider staffs and the bank staffs? Are you satisfied with currently outsourced services performance?
9. Is there any return back decision made on outsourced business process (interrupted, renegotiated, or prematurely terminated)? Why?
10. Is there a risk management framework for outsourcing by the bank? Does government has regulatory guideline on outsourcing?



# የኢትዮጵያ ንግድ ባንክ

## የፍላጎት መግለጫ ጨረታ ማስታወቂያ

ጨረታ ቁጥር 01/2010/2011/OMO

1. የኢትዮጵያ ንግድ ባንክ ከዚህ በታች የተዘረዘሩትን የአገልግሎት ዘርፎች አውትሶርስ አድርጎ በሌሎች ድርጅቶች ማሠራት ይፈልጋል። ስለሆነም በተመሳሳይ የአገልግሎት ዘርፍ የተሰማሩና አገልግሎቶቹን ለባንኩ ለማቅረብ ፍላጎት ያላቸው ድርጅቶች ቀርበው እንዲመዘገቡ ባንኩ ይጋብዛል።

አውትሶርስ የሚደረጉት የአገልግሎት ዘርፎች የሚከተሉት ናቸው፡-

1. የዕዳት አገልግሎት
2. የድምፅ እና ምስል ቀረፃ አገልግሎት
3. የሰው ኃይል ምልመላ እና መረጣ አገልግሎት
4. የማስታወቂያ አገልግሎት
5. የቢሮ እና የቴክኖሎጂ ዕቃዎች ጥገና አገልግሎት
6. የመልዕክት ማለዋወጥ አገልግሎት
7. የጥበቃ አገልግሎት
8. የተሸከርካሪ ጥገና አገልግሎት
9. ባንኩ በዕዳ ማካካሻነት የተረከባቸውን ንብረቶች የማስተዳደር አገልግሎት
10. የሕንፃ ማስተዳደር እና የጥገና አገልግሎት
11. የሕንፃ ግንባታ አገልግሎት
12. የሕንፃ ዲዛይን፣ ቁጥጥር እና የማማከር አገልግሎት
13. የቢሮ እና የቤት ዕቃዎች ጥገና አገልግሎት
14. የዕቃ እና አገልግሎት አቅርቦት አገልግሎት
15. የትራንስፖርት አገልግሎት

በጨረታው ለመካፈል የሚፈልጉ አካላት፡-

2. የአገልግሎት ዘርፉ የሚጠይቅ ከሆነ የሙያ ፈቃድ ከሚመለከተው የመንግስት አካል የተሰጣቸው፤ የታደሰ የንግድ ፈቃድ ያላቸው፤ የተጨማሪ እሴት ታክስ ተመዝጋቢ የሆኑ፤ እንዲሁም እንደ አገልግሎት ዘርፉ ከገንዘብ እና ኢኮኖሚ ልማት ሚኒስቴር የምዝገባ ሰርተፍኬት ያላቸው ሆነው እነዚህንም ሰነዶች ቅጅ በምዝገባ ወቅት ማቅረብ የሚችሉ መሆን አለባቸው።
3. የአገልግሎት ልምዳቸውን ሊያሳዩ የሚችሉ እና አገልግሎቱን በብቃት ለመስጠት የሚያስችል አቅም እንዳላቸው የሚያሳዩ ሰነዶችን ማለትም ከዚህ ቀደም በተመሳሳይ ዘርፍ ለሰጡት አገልግሎት የተሰጣቸው የመልካም ሥራ አፈፃፀም ማስረጃ ካለ፤ የድርጅቱን አስተዳደራዊ ተዋፅኦ እና ልምድ የያዘ አጭር መግለጫ፤ የሰው ኃይል እና የንብረት አደረጃጀት፤ እንዲሁም የድርጅቱን ወቅታዊ የፋይናንስ አቋም ወዘተ የሚያሳዩ መረጃዎችን እንዲያቀርቡ ይመከራል። ይህም መቅረቡ ባንኩ ለሚያደርገው የመጀመሪያ ደረጃ ብቃት ምዘናና መረጣ እገዛ ይኖረዋል።
4. በምዝገባ ወቅት ሙሉ አድራሻውን ማለትም ስልክ (ቋሚ እና ተንቀሳቃሽ)፣ ፋክስ፣ የፖስታ አድራሻ፣ የዌብሳይት አድራሻ (ካለ)፣ እና የኢሜይል አድራሻ በተጨማሪም የድርጅቱን ሕጋዊ ተጠሪ ስም እና አድራሻ መስጠት ይኖርባቸዋል።
5. ማስታወቂያው ከወጣበት ቀን ጀምሮ ዘወትር በሥራ ሰዓት ከሰኞ እስከ አርብ (ከ2:00-6:00 እና ከ7:00-10:00ሰዓት) እንዲሁም ቅዳሜ (ከ2:00-6:00ሰዓት) ሳሪስ በሚገኘው የኢትዮጵያ ንግድ ባንክ ንፋስ ስልክ ቅርንጫፍ ሕንፃ 3ኛ ፎቅ ቢሮ ቁጥር 314 አውትሶርሲንግ ማኔጅመንት ቢሮ በመምጣት መመዝገብ ይችላሉ። የምዝገባው ቀን ከ ነሐሴ 23 ቀን 2002 ዓ.ም. እስከ መስከረም 18 ቀን 2003 ዓ.ም የሚቆይ ይሆናል።
6. ከአዲስ አበባ ውጭ የሚገኙ አገልግሎት ሰጪዎች በአቅራቢያቸው በሚገኙ የባንኩ የዲስትሪክት ጽ/ቤቶች ከላይ የተጠቀሱትን ሰነዶች ይዘው በመቅረብ መመዝገብ ይችላሉ።
7. ለበለጠ መረጃ ከአውትሶርሲንግ ማኔጅመንት ቢሮ ፖ.ሳ.ቁ. 255 አዲስ አበባ፣ ስልክ ቁጥር 011 443 06 62 ወይም 011 443 09 80 እንዲሁም የፋክስ ቁጥር 011 4430861 ማግኘት ይችላሉ።

## DECLARATION

I, the undersigned, declare that this thesis is my original work, prepared under the guidance of Tilaye Kassahun (Phd). All sources of materials used for the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree.

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Name

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Signature& Date

## ENDORSEMENT

This thesis has been submitted to St. Mary's University College, School of Graduate Studies for examination with my approval as a university advisor.

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Advisor

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Signature & Date