THE EFFECTS OF PRODUCT DIFFERENTIATION STRATEGY ON CORPORATE GROWTH IN SELECTED MICROFINANCE INSTITUTIONS IN KENYA

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THE EFFECTS OF PRODUCT DIFFERENTIATION STRATEGY ON CORPORATE GROWTH IN SELECTED MICROFINANCE INSTITUTIONS IN KENYA

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Abstract

The main purpose of this study was to assess the effects of product differentiation strategy on corporate growth of Microfinance Institutions (MFIs) in Kenya. The study employed descriptive and quantitative research designs. The target population was 57 firms and the sample size was 32 firms arrived at through stratified and purposive sampling methods. The questionnaire was the primary data tool. The study found out that product differentiation strategy has significant effects on corporate growth in MFIs in Kenya. It concludes that increased deployment of product differentiation strategy increases corporate growth in MFIs in Kenya. It recommends that managers should create, protect and maintain differentiated products and services in order to be competitive in industry thus leading to corporate growth. Further, policy makers should find and implement ways of encouraging MFIs to create and maintain product differentiation in their portfolios.

Key word: corporate, differentiation, growth, product, strategy

1.1 INTRODUCTION

The growth of firms is something inherent to their actual existence. Throughout their life, firms must grow continuously if they want to sustain their competitive position within an environment where other rival firms may be growing at a faster pace (Johnson, Scholes & Whittington, 2008). While some surveys show that growth is not an objective for all firms, the ability of firms to grow is important, because it has been suggested that firms with low or negative growth rates are more likely to fail (Headd & Kirchhoff, 2007). What is perhaps more controversial and surprising is that recent evidence suggests that the high growth firms are not necessarily newly founded entrepreneurial startups, but rather tend to be larger and more mature firms (Honjo & Haranda 2006; Coad, 2009). Corporate growth leads to higher profits and increase in shareholders' value.

1.2 Corporate Growth and Differentiation Strategy

Product differentiation generates superior profitability for the reason that "[it] provides insulation against competitive rivalry because of brand loyalty by customers and resulting lower sensitivity to price. It also increases margins, which avoids the need for a low-cost position. The resulting customer loyalty and the need for a competitor to overcome uniqueness provide entry barriers. Differentiation yields higher margins with which to deal with supplier power, and it clearly mitigates buyer power, since buyers lack comparable alternatives and are thereby less price sensitive. Successful product differentiation leads to corporate growth.

2.0 LITERATURE REVIEW

A differentiation strategy calls for the development of a product or service that offers unique attributes that are valued by customers and that customers perceive to be better than or different from the products of the competition. The value added by the uniqueness of the product may allow the firm to charge a premium price for it. The firm hopes that the higher price will more than cover the extra costs incurred in offering the unique product. Firms that succeed in a differentiation strategy often have critical internal strengths: Access to leading scientific research, highly skilled and creative product development team, strong sales team with the ability to successfully communicate the perceived strengths of the product and   corporate

reputation for quality and innovation (Hitt, *et. al.,* 2012). When using differentiation strategy, a company focuses its efforts on providing a unique product or service. Since, the product or service is unique this strategy provides high customer loyalty. Product differentiation fulfills a customer need and involves tailoring the product or service to the customer. This allows organizations to charge a premium price to capture market share. The differentiation strategy is effectively implemented when the business provides unique or superior value to the customer through product quality, features, or after-sale support. Firms following a differentiation strategy can charge a higher price for their products based on the product characteristics, the delivery system, the quality of service, or the distribution channels. The differentiation strategy appeals to a sophisticated or knowledgeable consumer interested in a unique or quality product and willing to pay a higher price (Pearce & Robinson, 2013).

Differentiation consists in differentiating the product or service offered by the firm, in other words, creating something that is perceived industry-wide as being unique. Differentiation may be achieved in various ways, for example through design, brand image, technology, features, customer service, and dealer network. Bases of differentiation may be sorted into three categories. Firstly, to implement differentiation, a firm may focus directly on product (or service) attributes, i.e. product features, product complexity, timing of product introduction, or location. Secondly, a firm may focus on the relationship between itself and its customers, for example through product customization, consumer marketing and product reputation. Finally, differentiation may be implemented by focusing on the linkage within or between firms, which includes linkage within functions of a firm, linkage with other firms, product mix, distribution channels and service support. Ideally, the firm should differentiate itself along several dimensions (Porter, 2004; Rothaermel, 2015). Differentiation may generate superior profitability for the reason that "[it] provides insulation against competitive rivalry because of brand loyalty by customers and resulting lower sensitivity to price. It also increases margins, which avoids the need for a low-cost position. The resulting customer loyalty and the need for a competitor to overcome uniqueness provide entry barriers. Differentiation yields higher margins with which to deal with supplier power, and it clearly mitigates buyer power, since buyers lack comparable alternatives and are thereby less price sensitive. Finally, the firm that has differentiated itself to achieve customer loyalty should be better positioned vis-à-vis substitutes than its competitors.

Besides reducing the five threats of entry, rivalry, substitutes, suppliers and buyers, differentiation creates value by enabling a firm to charge a premium price that is greater than the extra cost incurred by differentiation (Valipour, *et. al*., 2012).

Creative firms will always manage to differentiate themselves from competitors. As rivals try to imitate these firms' last differentiation move, creative firm will already be working on new moves and therefore they always remain one step ahead of competition. In general, bases for differentiation that are costly to duplicate include links between functions, timing, location, reputation, distribution channels, and service and support. A differentiation strategy is appropriate where the target customer segment is not price-sensitive, the market is competitive or saturated, customers have very specific needs which are possibly under-served, and the firm has unique resources and capabilities which enable it to satisfy these needs in ways that are difficult to copy. These could include patents or other intellectual property, unique technical expertise, talented personnel, or innovative processes. Successful brand management also results in perceived uniqueness even when the physical product is the same as competitors. Sustained product differentiation leads to competitive positioning that leads to corporate growth (Johnson *et. al.,* 2008). New technologies improve efficiency, enable greater production, and are a source of profit for firms. Technological capabilities benefit firms in several ways: they enhance firm efficiency, reduce costs, and broaden market share, both locally and globally. Business that adopts greater levels of technological sophistication can be expected to grow more rapidly than a similar firm that don't. Low technological capabilities hinder and discourage firms from fully reaching their potential. In fact, firms with high levels of technological advancement tend to report high levels of corporate performance (Colombelli, 2014).

The effect of an increase in differentiation on market share is dependent on two opposing forces. On the one hand, an increase in differentiation most likely leads to a high cost position independent of scale, which result in a high average cost position ("cost increasing effect"). On the other hand, improved differentiation generates competitive advantage, which leads to increased market share, and following, to a low average cost position. Which one of the two forces dominates, and consequently, determines the total effect of improved differentiation on market share depends on the situation ("cost reducing effect"). Valipour, *et. al.,* (2012) notes that

differentiation should be translated into product improvement in order for the cost reducing effect to dominate. The reason is that an increase in product quality is believed to have beneficial effects on the relative product demand: When increased demand is addressed by mean of a raise in volumes, there may be indirect beneficial effects on relative direct cost position via a positive influence on market position. In other words, market share growth implies that economies may be achieved, which in turn results in reduced average costs (Porter, 2004; Hill & Jones, 2012). As differentiation increases, customers tend to become less price-sensitive, which allows firms to increase prices provided that differentiation does not induce costs which are superior to the price increase, profit margins increase. However, it is worth noting that differentiation does not need to be compromised by lower costs, provided that a firm can establish access to low labor costs. Differentiation leads to greater market share, provided that the product appeals to customers. This implies that a firm must identify and pursue customer preferences if it wishes to gain increased market shares through differentiation. More specifically, when customer preferences are favorable, differentiation allows a firm to expand its market shares via decreased price elasticity of demand (Porter, 2004; Valipour, *et. al.* 2012).

3.0 RESEARCH METHODOLOGY

This study used descriptive and quantitative research designs to establish the effects of differentiation strategy on the growth of MFIs in Kenya (Creswell, 2013). The target population was 57 firms (55 MFIs which are five years of age and above with operations in Mombasa County and two regulators, CBK and AMFI). Stratified sampling method was used to classify MFIs in three categories based on age; 5-10 years, 10-15 years and 15 years and above. The third category consisted of the regulators. Purposive sampling method was used to identify the 32 firms studied. Five questionnaires were distributed to each firm earmarked for study making a total of 160 questionnaires distributed. Validity and reliability were tested using Cronbach alpha and KMO and Bartlett test respectfully (Picardi & Masick, 2013). Data was analyzed both quantitatively and qualitatively. Descriptive statistics were generated. t-test, Regression analysis, and Anova were generated. Data was presented in tables.

4.1 DATA ANALYSIS AND INTERPRETATION

4.2 Response Rate

Out of the 160 questionnaires distributed, 114 were completed and received back hence the response rate was 71.25%. This response rate was sufficient for the study.

4.3 Reliability Analysis

Table 4.1 Reliability Analysis

Determinates of corporate growth	Reliability .	Cronbach's Alpha	Comments
Product Differentiation		.825	Accepted

The reliability analysis alpha score was .825 which was acceptable for this study.

4.4 Validity Analysis on Differentiation Strategy

The results of the factor analysis were shown in tables 4.2. The KMO measure of sample adequacy was 0.745 which indicated that the set of variables were suitable for factorization. Bartlett's test of sphericity was significant (Chi-square 480.630, p<0.000).

Table 4.2 KMO and Bartlett's Test for Differentiation Strategy

Kaiser-Meyer-Olkin Measure of	Sampling adequacy	0.745
Bartlett's Test of Sphericity	Aprox Chi-square	480.630
	Df	21
	Sig.	0.000

Table 4.3 illustrates the variance illustrated in differentiation strategy variables.

Table 4.3 Total Variance Explained for Differentiation Strategy

	Initial Eigen Values			Rotation Sums of Squared Loadings		
Component	Total	% of variance	% Cumulative	Total	% of Variance	% cumulative
1.	3.788	54.110	54.110	3.469	49.553	49.553
2.	1.075	15.352	69.462	1.394	19.909	69.462
3.	0.807	11.530	80.993			

4.	0.702	10.024	91.017
5.	0.382	5.452	96.469
6.	0.155	2.213	98.682
7.	0.092	1.318	100.000

Extraction Method: Principal Component Analysis

Principal component analysis with a Varimax rotation was used to factor analyze the seven items related to differentiation strategy. The correlation matrices among the items revealed a number of correlations in excess of 2 which meant that all responses were suitable for factorization. From the Variance matrix, there were two variables that had Eingen values of more than 1.0. This meant that these were the differentiation strategy variables that had the highest influence on corporate growth. Component one had the highest variance of 3.469 which accounted for 49.553% of the variance. Component 2 had the least variance of 1.394 and accounted for 19.909% of the variance. The cumulative results showed that there were two critical factors driving the use of differentiation strategy which accounted for 69.462% of the total variance in this construct. The other five factors also explained the variance at less than 30.538% which meant that some variance had been explained by latent variables.

In order to specify the number of factors that were influencing differentiation strategy and evaluate what variables to retain, factor loadings were taken into account and the minimum factor loadings were 0.646 which were considered to be moderately high. The factors affecting every one variable were all loaded up together and given a name so that the factors were reduced to a minimum of two. All the seven variables in differentiation strategy related to either factor 1 or 2 and were all retained for further analysis as shown in table 4.4

Table 4.4 Rotated Component Matrix for Differentiation Strategy

Differentiation Strategy Measures	Component	
	1	2
Wide branch network	0.740	
Grace payment period	0.646	

Customer service	0.772	
Mobile phone repayments	0.849	
Brand image	0.873	
Product innovation	0.652	
Service differentiation		0.936

Extraction Method: Principal Component Analysis.
Rotation Method: Varimax with Kaiser Normalization.
a. Rotation converged in 3 iterations.

From the rotation matrix in Table 4.4 a two factor solution was obtained explaining 69.462% of the total variance in differentiation strategy. These two factors were grouped as DS1 and DS2. DS1 had six items namely; wide branch network, grace payment period, customer service, mobile phone repayments, brand image and product innovation. This factor was named customer service. DS2 had only one item namely; service differentiation. This factor was named service differentiation. The results meant that all the constructs in product differentiation strategy were correlated to the two factors or they could be grouped into two.

4.5 Demographic analysis

Descriptive statistics for product differentiation strategy were generated and means evaluated against the questionnaires approximate survey value coded to the survey labels. The responses were mapped to questionnaires as; 1 = "No Extend", 2 = "Small Extend", 3 = "Moderate Extend", 4 = "Great Extend" and 5 = "Greatest Extend". The respondents' level of agreement on the effects of product differentiation strategy on corporate growth of MFIs in Kenya was generated as shown table 4.5.

Table 4.5 Product Differentiation on Corporate Growth

Statement	n	Mean	S.D
Wide branch network	114	4.17	0.911

Grace payment period	114	3.19	0.458	
Customer service	114	3.21	0.451	
Mobile phone repayments	114	3.47	0.552	
Brand image	114	4.28	0.672	
Product innovation	114	3.67	0.687	
Service differentiation	114	3.47	0.833	
Grand	114	3.64		

Majority of respondents agreed that brand image strongly affected corporate growth of MFIs in Kenya with highest mean score of 4.28. Further, more respondents indicated that wide branch network increased market share and thus increased corporate growth with a mean of 4.17. A notable number of respondents agreed that product innovation greatly increased corporate growth in MFIs in Kenya with a mean score of 3.47. The inferential statistics indicate that an overall mean score of 3.64 (inferring to survey value (4), coded as great extend) was achieved for effects of differentiation strategy on corporate growth of MFIs in Kenya. Differentiation is a key strategy in highly competitive industries as the case with the MFI sector.

4.6 t –Test on Product Differentiation Strategy Measures

Differentiation strategy objective was assessed by seven measures and after factor analysis all these measures were retained namely; wide branch network, grace payment period, customer service, mobile phone repayments, brand image, product innovation and service differentiation. The significant results showed that the means were statistically different and the alternative hypothesis was accepted. The means of all these constructs have been identified in Table 4.6.

Table 4.6 t –Test on Differentiation Strategy Measures

Differentiation Strategy Measures	Sample Size (N)	Mean	Std Error Mean	t-value	Significance (P-value)
Wide branch network	114	4.167	0.085	48.820	0.000

Grace payment period	114	3.193	0.043	74.356	0.000
Customer service	114	3.211	0.042	76.068	0.000
Mobile phone repayments	114	3.474	0.052	67.200	0.000
Brand image	114	4.281	0.063	68.022	0.000
Product innovation	114	3.667	0.064	56.985	0.000
Service differentiation	114	3.474	0.078	44.521	0.000

Overall mean score = 3.638 t-test for equality of means: t-value = 0 = (Ha: there was no difference expected between the means, at α = 0.05, 2-tailed). Reject Ha if P-value ≤ α , otherwise fail to reject Ha if P-value > α .

Table 4.6 presents the t-Test results which show that on a scale of 1 to 5 (where 5 = to Greatest Extent; 1 = No Extent) differentiation strategy to a great extent was influenced by brand image (mean score = 4.281), wide branch network (mean score = 4.167), and product innovation (mean score = 3.667) and to a moderate extend by mobile phone repayments (mean score = 3.474). On average, the effects of differentiation strategy on corporate growth was to a great extend (overall mean score = 3.843). The one sample t-test comparisons of differentiation strategy mean scores indicates differences that were all statistically significant. This implies that the extent of effects of differentiation strategy on corporate growth varies from firm to firm with the highest difference score noted in customer service (t-value = 76.068, P< 0.05), followed by grace payment period (t-value = 74356, P< 0.05) and brand image (t-value = 68.022, P< 0.05). The lowest statistical difference was reported in service differentiation (t-value = 44.521, P< 0.05).

4.7 Regression Analysis

The regression analysis was modeled to measures how well our overall model fits, and how well Product Differentiation is able to predict Corporate Growth. The linear regression analysis modeled the relationship between the dependent variable (Corporate Growth) and independent variable (Product Differentiation).

4.7.1 Overall Goodness of Fit

The regression model summary gives the measures of how well one's overall model fits, and how well Product Differentiation is able to predict Corporate Growth. R is a measure of how well predictors predict the outcome, but the study needed to take the square of R (R^2) to get a more accurate measure. This gives the study the amount of variance in corporate growth explained by the Product Differentiation or predictors. The R^2 varies between 0 and 1. In the study R = .343, representing a 34.3% of the variance in Corporate Growth can be explained by Product Differentiation, although this does not imply causality. The final column gives us the standard error of the estimate. This is a measure of how much R is predicted to vary from one sample to the next. An R^2 = 1 indicates that the regression line perfectly fits the data. In Table 4.7 below, an R^2 = .343 indicates that the regression line moderately fits the data. Using the enter method it was found that the strategic management determinates explain a significant amount of the variance in the value of Corporate Growth (F(6, 107) = 58.520, p < .05, R^2 = .343, R^2Adjusted = .337).

Table 4.7 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.586[a]	.343	.337	.22152

a. Predictors: (Constant), Strategic Synergy, Resource Pooling, Grand Strategy, Cost Leadership, Product Differentiation, Corporate Vision

b. Dependent Variable: Corporate Growth

4.7.2 Analysis of Variance

In its simplest form, ANOVA provides a statistical test of whether or not the means of several groups are equal, and therefore generalizes the t-test to more than two groups. The F test (Fisher F distribution) is the ratio of two variances, which are used to determine if two variances are equal. In Table 4.8 the numerator df (1) tells how many predictors the study had (i.e. Product Differentiation) and the denominator degrees of freedom (113 – 1 = 113) for bi-variate regression use. The value of the F test is $F(1,112) = 58.520$, ($p < .05$). This means the value of F is statistically significant at a level of 0.01, which suggests a linear relationship among the variables. The statistical significance at a 0.01 level means there is a 99 percent chance that the relationship among the variables is not due to chance.

Table 4.8 ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.872	1	2.872	58.520	.000[b]
	Residual	5.496	112	.049		
	Total	8.368	113			

a. Dependent Variable: Corporate Growth

b. Predictors: (Constant), Strategic Synergy, Resource Pooling, Grand Strategy, Cost Leadership, Product Differentiation, Corporate Vision

4.7.3 Simple Regression Results of Product differentiation Strategy on Corporate Growth

The regression coefficient is the slope of the regression line. It gives the information for writing the regression equation. The slope is how steep the line regression line is. A slope of 0 is a horizontal line, a slope of 1 is a diagonal line from the lower left to the upper right, and a vertical line has an infinite slope.

Table 4.9 Simple Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.973	1.63		12.131	.000
	Product Differentiation	.339	.044	.586	7.650	.000

The intercept is where the regression line strikes the Y axis when the independent variable has a value of 0. The study had one predictor variable (Product Differentiation). Therefore, a linear regression model with one predictor variable can be expressed with the following equation:

$$Y = \beta_0 + \beta_1 * X_1 + e.$$

The parameters in the model are β_0, the Y-intercept (Constant = 1.973); β_1, the regression coefficient (product differentiation Strategy = .586). Therefore, the final equation can be expresses as;

Y= 1.973+.586x

This basically means that with one unit change in differentiation strategy, corporate growth can be predicted as;

Y= 1.973 + .586(1); Y = 2.559

4.8 Discussions

The findings revealed a statistically significant positive relationship between product differentiation strategy and corporate growth. Service differentiation, brand image and mobile repayments were key contributors to firm differentiation. This implies that if MFIs immensely increase product differentiation, corporate growth increases. This basically encourages MFIs managers to highly differentiate their products and services. Worth noting is that firms that succeed in differentiation strategy have critical internal strengths that can cover for the high prices of differentiation. Johnson *et. al.,* (2008) post that differentiation strategy is appropriate when the customers are not price-sensitive, market is competitive and saturated, customers have specific needs that are under served, and the firm has unique resources and capabilities that are unique to copy.

5.1 CONCLUSIONS AND RECOMMENDATIONS

5.2 Conclusions

This study concludes that increased deployment of product differentiation strategy increases corporate growth in MFIs in Kenya. Basically, with an improvement in use product differentiation strategy, corporate growth increases profusely. It is therefore the firm's responsibility to deploy the best mix of product differentiation strategy subvariables and put them into practical perspective for corporate growth to be realized in MFIs in Kenya.

5.3 Recommendations

This study recommends that managers should create, protect and maintain differentiated products and services in order to be competitive in industry thus leading to corporate growth. Further, policy makers should find and implement ways of encouraging MFIs to create and maintain differentiation of their products and services.

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