

Competitive Threats and Diversification In Mexican and European Bank Markets

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ABSTRACT

This paper examines the effectiveness of strategic planning in commercial banks and how management styles influence (or reflect influences) on diversification decisions within bank markets. The research is based on and further develops a framework proposed by Goold and Campbell (1987) and Goold *et al.* (1994) by testing the strategic response of banks to changes in their growth opportunities. Changes in growth opportunities are measured by diversification and market positioning moves that respond to external innovations (and in particular to changes in regulation and IT applications). External change is, therefore, thought to have introduced strategic needs to bank markets through effective threats of entry and to have resulted in several dimensions for commercial banks as new intermediaries diversified into bank markets.

Empirical support for the effectiveness of strategic planning emerged from interviews with senior managers with direct (and indirect) responsibilities in bank markets and working within distinct competitive environments. The first part of the survey was carried out in 1996 in Mexico, Spain and the UK. The second part considered Germany, Ireland and Mexico in 1999. A third survey considered participants from Sweden, Estonia and Portugal in 2001.

Results emerging from triangulating responses suggested that, on balance, top managers in bank markets are predisposed to integrate around purely strategic rather than purely financial targets or than a combination of strategic and financial performance. Management of diversity does not seem to be time invariant with results suggesting that technological advances have increased in importance from rank 5 in 1993, to rank 3 in 1996, and top of the list in 1999 and 2001.

At the same time, the analysis established that diversification moves of domestic competitors (resulting from regulatory and technological innovations) rather than newly established foreign banks, were perceived as the top drivers to change the boundaries of bank markets. Information technology management played a secondary role in the design of bank strategy but at the same time, computer applications were perceived as an important force to modify competition in bank markets.

Keywords: Banks, Corporate Strategy, Diversification.

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INTRODUCTION

Over the last two decades, there have been many studies on the degree of competition in banking. These studies have aimed to assess whether external change modified barriers to entry and exit bank markets. At the same time, empirical support was also sought to determine whether external change produced effective threats of entry into banking (see further Gilbert, 1984, p. 643; Gardener and Molyneux, 1990, p. 98; Heffernan, 1996, p. 219 or Humphrey and Pulley, 1997, p. 83). An overwhelming number of research studies, however, have focussed only on changes in formal profitability and banks' cost structures, disregarding other influences on profit variations such as changes in managers' abilities or in the strategic goals and objectives of senior managers of banks. Studies looking at changes in formal profitability and banks' cost structures were inconclusive about the role that visionary strategies play in explaining changes in individual banks' size (economies of scale), scope (breadth of business) and diversity (shared resources) as a response to deregulation and technical change (Gilbert 1984, p. 643; Muda, 1993, p. 39; Gardener, 1995, p. 1 and Heffernan, 1996, p. 135). Moreover, empirical support failed to materialise and explain whether to cope with external changes senior managers of banks exert effective control of distinctive resources such as organisational skills, capabilities and other intangible assets.

The research project described here devised and tested an approach based on Goold and Campbell (1987) and Goold *et al.* (1994) to assess the response of bank managers to external change. In particular, the study aimed to establish whether, as a response to external innovations, managers selected the best growth opportunities; effectively implemented strategic change to enter new markets; and as a result, whether banks gain a competitive edge for reasons other than fortuitous events or tactical strategies. The research project then considered whether diversification-based growth deals with finding stable income streams through a combination of activities that achieve large reductions in unsystematic risk (Gardener and Molyneux, 1990, p. 217). At the same time, growth through synergy will occur when profitability improves over the simple adjoining of independent activities (Ballarín, 1985, p. 50). Ultimately, then, this research presents direct and indirect support the suspicion of among others Baker (1997, p. 6) and Knights *et al.* (1997, p. 17-18 and 20-23) that participants in the markets for financial services and commercial banks in

particular, place greater emphasis on profit related goals (i.e. supplied oriented) than growth driven by the satisfaction of customer “needs” (i.e. customer-oriented approach).

The paper proceeds as follows. The next section offers a frame of reference to the analysis of banks’ strategic planning decisions and diversification moves. The third discusses the methodology used in the semi-structured interviews. The fourth encompasses the qualitative analysis of interviews. The final section presents a summary and tentative conclusions.

THE DESIGN OF STRATEGY IN BANKING: AN ANALYSIS FRAMEWORK

Since the late 1970s financial service organisations have observed reduced rates of financial return, raised fees for deposit services, reduced branch operating costs and a shift to higher earning assets. In other words, external innovations (and in particular, regulatory change and IT applications) were instrumental in the changes banks made to their balance-sheet size, in increasing business-portfolio diversity and in restructuring their geographic scope (Gardener and Molyneux, 1990, p. 98). Changes in the size and diversity of banks followed external changes in bank markets but banks’ strategic responses were still short of the competitive (or perfectly contestable market) benchmark (documented in Bank of England, 1991, Dickens and Phillipatos, 1994 and de Bandt and Davis, 1999). Documented evidence would thus suggest that some of the changes increased competition in bank markets while some others pursued strategies aiming to deter new participants entering the market (such as deterring insurance companies to supply unsecured lending).

According to Gardener and Molyneux (1990, p. 214), Walter (1997, p. 345) and Canals (1998, p. 624), the strategic response of commercial banks in Western Europe in light of changes in their growth opportunities during the late 1980s was to adopt two main generic strategies or types of organisational design. One set of banks adopted wide spread diversity in their geographic, product market and customer group portfolio. Whilst another set followed a rather focused strategy by specialising in one or all of those dimensions. According to Demsetz (1973, p. 3) and evidence documented in Gilbert (1984, p. 628), Walter (1997, p. 345) and de Bandt and Davis (1999, p. 17), banks of different sizes and operating in distinct markets reflected different levels of efficiency. Two main explanations are possible. The first explanation is that of different degrees of competition across markets, that is, banks facing different barriers to entry and exit. Different degrees of competition would suggest the possibility of distinctive external growth opportunities based on geographical location. Location would then provide an explanation for bank size and relative

efficiency because external growth opportunities are opened up by regulatory change, technical innovation, developments in the degree of market competition (market structure), and changes in customer preferences.

The alternative explanation is that banks' generic strategies are based on an internal or production-function perspective. Internal growth opportunities for commercial banks depend on the ease with which operating efficiencies, scale economies and scope economies can be exploited (Walter, 1997, p. 345). In other words, bank managers decide on the scope of the banks' activities by weighing up the advantages of scale and scope against those of flexibility, simplicity and specialisation (Canals, 1998, p. 626).

Among others Walter (1997, p. 347 and 350) and Guillén and Tschögl (2000) have documented empirical evidence suggesting that there is no inherent advantage built into generic organisational profiles for banks. Banks of the same size and with the same breadth of geographic, product market and customer group are known to observe different cost structures (Domenech *et al.*, 1993, p. 97; Walter, 1997, p. 350). Instead of generic strategies, differences in banks' market position or cost structures are thought to be based on bank managers anticipating the most attractive markets and capturing greater shares of growth opportunities by effective execution (of a visionary course of action). Bank senior executives actively engaged in strategic planning could have forecasted the most profitable growth alternative for their banks and considered whether to enhance established capabilities to compete, create new capabilities or divest established capabilities (as market-based transactions or non-bank providers could be more efficient brokers of funds). Since the combination of anticipation and implementation is the source of sustainable competitive advantage, then differences in banks' cost structures or market positions emerge as anticipated advantage creates capabilities to compete. Unfortunately there is little systematic evidence that banks which engage in strategic planning outperform those that do not (Muda, 1993, p. 22; Kaplan, 1994, p. 56; Gardener, 1995, p. 1 or Newkirk Moore, 1995, p. 335), with the added result of having little empirical support to determine whether differences in planning approaches are responsible for distinct sets of capabilities to compete in bank markets.

In light of little systematic evidence on the effectiveness of banks' planning schemes, the research project proceeded based on the possibility that strategic and financial control of capabilities develops into a competitive edge. This link between strategic intent and core capabilities was originally put forward by Penrose (1959, p. 110) and successfully measured by Rumelt

(1974). Surveys of the literature exploring Penrose's propositions for firm growth are found in Ramanujan and Vadarajan (1989), Conner (1991) and Schulze (1994). From the surveys it emerges that Penrose's main proposition was that strategic intent will rank resources, dedicated assets, intangible assets, skills and other inputs into the production process which determines the ability of a firm to compete. The purpose of the ranking is to establish which resources and which capabilities will allow the firm to capture the most promising growth opportunities. Strategic intent will also determine whether the firm must develop new capabilities or resources and whether the firm must change co-ordination and co-operation patterns between people, and between people and resources (Grant, 1991, p. 22).

Strategic intent, therefore, establishes which resources and capabilities will be key for future profitability and these profit generating resources and capabilities are called "core capabilities". Furthermore, high strategic and financial control of core capabilities provides the organisational flexibility that visionary strategies require to deliver high sustainability of competitive advantage.

Participants in bank markets are thus defined as banks, non-banks and non-finance intermediaries willing (and able) to develop a set of core capabilities closely related to brokering the financial needs of low-volume surplus- and deficit-spending agents as well as maintaining a national payment system. This set of distinctive capabilities represents the basis for competition in core markets for commercial banks.

Financial service organisations can also be defined from a consumer perspective. According to McKechnie (1992, p. 65) and Lewis (1994, p. 270), there are two service quality expectations that distinguish financial services, namely fiduciary responsibilities and two-way information flows between bank and customer. Firstly, fiduciary responsibilities refer to the responsibility that financial service organisations have regarding the management of their customers' funds and the nature of the financial advice supplied. Secondly, two-way information flows reflect individual customers repeatedly purchasing the same service from the same financial service organisation, sometimes over extended periods of time. Financial transactions and particularly those in retail bank markets require a great deal of information that reflects the latest changes in customers' private and confidential financial status (op. cit.).

The research project was then poised to determine whether growth opportunities in bank markets are captured through new establishments or through diversification moves of established participants. Empirical evidence documented in Geroski (1995, p. 426), however, suggested that

opportunities are captured by diversification (creating or relocating capabilities) rather than new establishments because capital building from scratch to effective competition threat is not, on average, very successful or even likely. Indeed, Caves and Porter (1977, p. 241) was the first to suggest that greater competitive threats were distinguishable between the in-market and out-of-market competitors. Moreover, these studies make an implicit claim that entry barriers affect the choice of diversification into bank markets (see further Ramanujan and Vadarajan, 1989, p. 269 or Yip, 1982, p. 332).

In other words, the analysis of entry and diversification strategies into bank markets can establish a causal link in the relationship between growth opportunities, strategic change and core capabilities. This paper, therefore, follows documented research on analysis of entry and diversification to centre on establishing which are the feasible organisational structures or management practices that achieve a competitive edge in bank markets. Insights will emerge through the discussion of the intent behind developing capabilities to compete at high- or low speed through diversification moves. Insights will develop as it is expected that the analysis of broadly defined diversification will shed light into how bank managers confront external change and overcome entry barriers to achieve sustainable competitive advantage.

There are several alternatives to benchmark external parameters and indicators that link management practice and competitive advantage creation. However, grounded work by Goold and Campbell (1987) and Goold *et al.* (1994) are among those studies which claim that the potential response to growth opportunities is associated with a reduced number of managerial practices. Variety is reduced though management styles establishing, first, whether top executives consider contributions of middle managers when looking for growth opportunities and second, establishing whether top executives consider that competitive advantage will emerge from integrating activities around financial or strategic objectives. Table 1 summarises the strategic styles and their relationship with a particular form of control and set of performance objectives (Goold and Campbell, 1987, p. 46 and Goold *et al.*, 1994, p. 412). The first of these styles is Financial Control encompassing senior managers who believe better management emerges from top executives setting tight expenditure objectives or strict performance targets and thus, leave most planning decisions to business unit managers. The second style is called Strategic Planning which is identified with an authoritative CEO or a group of top managers who integrate business activities round strategic targets (such as market share) and thus, cross-subsidise activities (i.e. high-financial return

businesses finance low-return businesses while the latter achieves its strategic goals). The third style is called Strategic Control and represents senior managers who believe in the active influence and participation of business-unit managers in discovering growth opportunities. Strategic Control managers aim to strike a balance between market performance and resource allocation within the organisation.

Table I: Type of Growth and Management Style

<i>Objective</i>	<i>Enforce by</i>	<i>Style</i>	<i>Core capabilities perceived as:</i>	
			<i>Platform-based</i>	<i>Unique (Specific to the bank)</i>
Financial	Tight (Centralised) Control	Financial Control	-Geographic concentration.	-Geographic diversification.
			-Product-market diversification.	-Consolidation of business lines.
			-Customer group diversification.	-Customer group diversification.
Strategic	Flexible (Distributed) Control	Strategic Control	-Narrow geographic span.	-Narrow geographic span.
			-Focus on product markets.	-Focus on product markets.
			-Customer group diversification.	-Customer group specialisation.
Financial and Strategic	Tight (Centralised) Control	Strategic Planning (Prominent Person)	-Geographic diversification.	-Product market diversification.
			-Product-market diversification.	-Narrow geographic span.
			-Customer group diversification.	-Narrow customer group business.
	Flexible (Distributed) Control	Strategic Planning (Distributed Approach)		

Source: Goold and Campbell (1987), Goold *et al.* (1994), and authors.

There are two elements to the criteria used by these management styles to assess diversification moves. The first element is that diversification must be expected to create value, either from the new business to the parent company or vice versa. The second element is that through diversification the parent organisation must be expected to add more value to the new business than any other potential parent (Goold and Campbell, 1991, p. 116 and Reiton and Foote, 1988, p. 49). These two elements are necessary conditions for competition and suggest that strategic styles reflect (rather than cause) competitive advantage. These two elements to assess diversification moves also point towards patterns of behaviour, which is useful in identifying traits in how strategy is formulated

and to identify which features of growth are particular to each style of management (Goold and Campbell, 1987, p. 161). Namely:

- ❑ Strategic Planning style companies favour organic growth (i.e. increase core capabilities);
- ❑ Financial Control style companies tend to favour diversification through acquisitions; while
- ❑ Strategic Control style companies also favour growth through core capabilities but balance this growth with consolidation or divestiture of non-performing businesses and as a result, maintain without change the overall dimension of the firm.

Growth features associated with management styles have an implication on the type of diversification or repositioning move each style is likely to adopt as a response to external change. Each management style will pursue different diversification moves that create (or consolidate) either new stand alone businesses, businesses that enhance core capabilities or businesses that are strategic complements to on-going activities. The particular tendency each style develops is based on anticipated advantage and how visionary strategies predispose managers to consider first, core capabilities as unique to business units or as a broad platform for growth (see some empirical support in Bátiz-Lazo and Wood, 1999) and secondly, whether diversification or market positioning moves follow visionary strategies aimed at capturing economies of scale or economies of scope.

Table 1 also shows the generic strategies associated with each management style. These are based on bank senior managers' perception of core capabilities and scale and scope economies are hypothesised to be as follows. Geographic concentration together with product-market and customer group diversification seem more likely for Financial Planning style banks where capabilities are perceived as a broad platform for growth. Patterns of scope diversification emerge as profit generating resources associated with managers' ability to transfer proprietary information (intangible capabilities such as "Know-How") to alternative activities at lower costs than those incurred by independent business units (Teece, 1980, p. 226). On the other hand, Financial Control style managers that perceive core capabilities as associated with specific or unique profit generating resources seem likely to complement geographic diversification with business line consolidation to capture benefits that should emerge associated with scale economies.

Banks managed under Strategic Planning styles seem likely to be less concerned with potential entrants (than those at Strategic Control banks) because of their slower reaction to divest poor

performing business (Goold and Campbell, 1987, p. 160). Such concerns suggest Strategic Planning style banks will assign relatively longer time spans to strategic investments and thus, for diversification or market positioning moves to achieve profitability. A predisposition to universal and even global banking seems more likely for Strategic Planning style banks that perceive core capabilities as a broad platform for growth rather than those banks building upon a perception of capabilities as a unique set of resources. For Strategic Planning style banks building on a unique perception of core capabilities, achieving scale through product market diversification will be more attractive.

Banks managed under Strategic Control styles will assign longer time spans for projects based on "core" or "strategically important" capabilities than to "stand alone" capabilities because Strategic Control style management favours maintaining without change the overall dimension of the firm. The perception of capabilities as a broad platform for growth will favour the pursuit of scope economies and will be followed by customer group diversification. Strategic Control style banks that perceive core capabilities as unique are likely to focus on specific customer segments and thus, try to capture scale economies. As mentioned above, Strategic Control style managers do not seem concerned with firm-size growth, therefore the response of Strategic Control style banks to deregulation and IT innovation seems likely to be the pursuit of scale or scope economies based on a narrow geographic span and focus on product markets.

In summary, anticipated advantage can provide banks with access to a unique set of capabilities before or after regulatory and technological change. However, in light of little systematic evidence on the effectiveness of banks' planning schemes, the research project proceeded based on the possibility that strategic and financial control of capabilities develops into a competitive edge. Empirical evidence will then help to establish the effectiveness of anticipating advantage in bank markets. Also whether providing access to unique capabilities results in greater competition in bank markets. This as measured by banks' overwhelming response to external change being geographic and customer group diversification rather than product market diversification of new and potential entrants. Growth in bank markets will reduce bank growth because as long as banks can preserve and develop their stock of unique capabilities then actual or new competition will be irrelevant to implementing visionary strategies. Visionary strategies that enhance banks' core capabilities will, therefore, pre-empt competition from non-bank and non-finance intermediaries. In other words, the possibility that strategic intent provides banks with unique capabilities has direct implications on how

senior managers control their banks' profit generating processes to anticipate high sustainability of competitive advantage in bank markets.

In the following sections, research project offers some evidence for the relationships between anticipated advantage, diversification, the development of core capabilities and performance in bank markets. This evaluation is based on interviews with managers from distinct competitive environments, who had direct and indirect responsibilities in bank markets.

RESEARCH METHODOLOGY AND DESIGN OF INTERVIEW SCHEDULE

Questionnaire Design

The initial design phase of the interview schedule began in February 1995. This stage encompassed six separate in depth interviews with bank CEOs and heads of planning. These interviews provided a basic agenda on the major areas of concern for commercial banks and were the basis for the design of a formal interview schedule. Consensus between open-ended interviews developed into five broad areas of corporate strategy that needed to be addressed by the interviewer administered questionnaire, namely:

- ❑ Diversification decisions (i.e. disposing or acquiring business lines);
- ❑ Assessing actual and potential competitors;
- ❑ Critical events (i.e. moments at which options exercised to pursue major change in operations);
- ❑ Elements establishing where and how the bank would compete; and
- ❑ The nature of banking in the future (centred on the idea of diversification).

From those initial areas of concern three sections of inquiry were developed to establish the origins and effectiveness of strategy. The five areas mentioned above were contained within the three sections as follows:

- ❑ Financial dimensions of strategic investment decision. The dimensions provided a basis to extract information on how managers implemented diversification and market positioning moves to develop new businesses, new product markets or to meet the needs of new customer groups.

- Criteria for competitive positioning which included an assessment of how and when major changes in operation responded to deregulation and information technology (IT) innovations; and
- Establishing managers' perceptions of the (main) future determinants of competition in bank markets. Managers identified how actual and potential competition acted as driver of strategic change.

Each section revolved around a handout although the semi-structured nature of the interview allowed questions to be reworded. Rewording questions was important as the interviewer anticipated that previously unconsidered areas would emerge in the course of the discussion (Gordem, 1975, p. 74 and Belson and Duncan, 1978, p. 160). 1978, p. 160). When ready, the questionnaire comprised 44 questions with a potential of 68 separate answers (per interview). The modal response rate was 41 questions (minimum 1 and maximum 55) while the overall response rate to questions was 55% of the total.

Interview sessions were scheduled to last between 45 and 75 minutes, although in some instances the open ended format resulted in interviews as long as two hours. All sessions were taped and transcribed verbatim. Only two interviews took place on the telephone, the remainder were face to face. On eight occasions (7%) two or more persons made joint contributions but their answers were considered as that of a single respondent. In total, 20% of the schedule was prompted in check-list form. An average 87% of the total number of close-form responses prompted adequate constructs (to measure strategic planning in banks and diversification moves in bank markets).

On average, one out of six interviewees redefined the alternatives prompted. Results suggest that, on balance, the questionnaire had a firmer grasp of constructs measuring banks' strategic planning processes than of constructs measuring diversification and market positioning moves. These results emerged as constructs into banks' strategic planning processes had fewer innovations (12% of total responses) than those into bank diversification moves (16% of total responses). As a result, the analysis was able to make a distinction between product market moves (reflecting a response to liquidity changes within the broad economic cycle) and diversification or repositioning moves (reflecting long-term responses to change in the attractiveness of product markets).

The interview schedule was written in English and aimed to avoid technical terms (following Moser and Kalton, 1978, p. 141). The schedule was translated into Spanish, Portuguese and German using, as far as possible, equivalents to operational concerns. The interview schedule used a different term for non-English speaking interviewees in the absence of a colloquial equivalent “core capabilities”, that is, “capacidad intrínseca” in Mexico, “capacidades esenciales” in Spain, “capacidades centrais” in Portugal and “Kernfähigkeit” in Germany (see further Bátiz-Lazo and Wood, 1999). The interview schedule was also compared to that from a survey of 400 of Europe's successful banks and capital market players. The original was a postal survey carried out by Arthur Andersen in 1993 and designed to establish attitudes towards the “forces of change in financial markets” (as documented in Gardener, 1995, p. 3). During the interviews a handout presented the list of constructs emerging from the 1993 survey and prompted interviewees to re-rank them in order of importance.

Sample Characteristics

Table 2 shows the geographic distribution of the 115 interviewees, which included 55 participants (48%) from Mexico, Spain and the UK. This first set of interviews took place mainly between April and July 1996, but with some interviews taken place as early as March or as late as October. The second set consisted of 38 participants (33%) from Ireland, Germany and Mexico, and mainly took place between March and June 1999, but with some taking place as late as November and December. The third set consisted of 22 participants (19%) from Sweden, Estonia and Portugal, which took place in January and May 2001. Nineteen persons (17% of the total) answered a shorter version in writing and these responses were used exclusively for the qualitative assessment.

Table 2 also shows the sector distribution interviewees, which included 67 managers of commercial banks (58%), 11 managers at savings banks, co-operative banks or building societies (10%). All these 78 participants belonged to the three top levels of management. At the same time, the requirement was that they had more than two years of direct involvement in the design of strategy at regional, national or international level.

The second sector group had direct experience with the banking sector but no current responsibilities. This sample included 22 sector specialists from investment banks (19%), 12 management consultants (10%) and 3 bank regulators (3%). Sector specialists were either in the

sample country or at the London office of the investment bank. Management consultants were Partners or Project Managers (in all but one case, from a “Top 6” firm), with again a minimum of two years experience in servicing commercial banks. Regulators had experience in the central bank's research or external audit departments. The result of this careful screening was that all interviews were productive in that they produced credible and internally consistent responses that reflected a sound knowledge of bank strategic management.

Table II: Sector and Geography Distribution of Participants in Survey (1996, 1999 and 2001)

		1996				1999				2001	
		<u>Sector</u>				<u>Geography</u>				<u>Sector</u>	
Commercial	24	44%	Mexico	14	12%	Commercial	27	71%	Ireland	11	10%
Investment	14	25%	Spain	23	20%	Investment	5	13%	Germany	10	9%
Consultant	8	15%	UK	18	16%	Consultant	1	3%	Mexico	17	15%
Saving bank	6	11%				Saving bank	5	13%			
Central bank	3	5%				Central bank	0	0%			
<i>Sum</i>	55	100%	<i>Sum</i>	55	100%	<i>Sum</i>	38	100%	<i>Sum</i>	38	100%
		<u>Sector</u>				<u>Geography</u>				<u>Sector</u>	
Commercial	16	73%	Portugal	13	11%	Commercial	16	73%	Portugal	13	11%
Investment	2	9%	Estonia	3	3%	Investment	2	9%	Estonia	3	3%
Consultant	3	14%	Sweden	6	5%	Consultant	3	14%	Sweden	6	5%
Saving bank	1	5%				Saving bank	1	5%			
Central bank	0	0%				Central bank	0	0%			
<i>Sum</i>	22	100%	<i>Sum</i>	22	100%	<i>Sum</i>	22	100%	<i>Sum</i>	22	100%

Market participants in different countries were selected to illustrate how similar regulatory changes and IT innovations were adopted in five different competitive environments. Surveying organisations in the European Union would allow insights into a process that:

"..really began in Western financial systems during the late 1960s and early 1970s. This ‘path’ is characterised *inter alia* by the widespread adoption of ‘free market economics’ ... [a]

certainly remarkable commitment by Western (and increasingly other) governments..." (Gardener, 1995, p. 1).

The benchmark was the UK because this country always had a large and highly competitive wholesale banking markets, and preceded other countries in regulatory change (as documented by Bank of England, 1991). The UK was also an early adopter of dual process of increasing competitive pressures and imposing supervisory, investor protection and conduct of business rules in bank markets. A fixed exchange rate regime (part of the Bretton Woods international monetary agreement) was abandoned in 1979. That same year, Paul Volker, then chairman of the Federal Reserve System (i.e. the US Central Bank), modified the long-standing policy of fixed or sticky interest rates and adjustments of the money supply to the business cycle. Instead, active use of interest rates was introduced to enact direct control of the money supply. UK regulators were amongst the first to follow the move and allowed domestic interest to float and vary according to market forces. Participants in UK bank markets were also seem to have adopted key technology innovations before the Mexican or Spanish banking markets (as documented by Solís and Trigueros, 1991, Gardener, 1995, p. 4 and Guillén and Tschoegl, 2000).

At the same time, the regulatory change timetable in Spain accelerated during the 1980s to catch up with the EU Single Market, providing an example that was regarded as interesting and one of uncertain impact on the competitiveness of the banking sector (as documented by Lloyd-Williams *et al.*, 1994). According to Canals (1994, p. 84) and de Bandt and Davis (1999, p. 14), in Germany competition in loan markets seems more intense than for fee-generating activities, while overall activities are short of the overall competitive benchmark. Irish bank markets were interesting as they have been influenced by developments in the UK and the EU Single Market as well as the drive to attract direct foreign investment and create an international financial centre in Dublin. Changes in Mexican markets were introduced to allow collecting comparable data on changes in growth opportunities internal to Mexico and corroborated sector-wide phenomena common to all bank markets (as opposed to effects specific to a region or country). Changes in Mexican markets followed other countries as market driven interest rates and unrestricted credit allocation were phase into domestic markets after 1989 while the government had management and share capital control of commercial banks until 1992. In all cases, however, interviewees represented more than 60% of the total assets in each country.

As documented by Foddy (1993, p. 82) and Bowman and Ambrosini (1997), the risk of inferences into strategic behaviour based on single source responses of an organisation is avoided by introducing individuals of the same institution as interview sources. Hence, to achieve the proper level of social generality of responses in 63 cases (55%) respondents were members of the same institution although working at a different location or in a different line of business (i.e. retail or investment banking). Including participants based in provincial cities and working in medium- and small-sized increased the diversity of responses and aimed to strengthen triangulation throughout the research (Yin, 1984, p. 48; Eisenhardt, 1989, p. 537; Robson, 1993, p. 290; among others.) Again, triangulation with several sources helped to corroborate sector-wide phenomena common to all bank markets as opposed to effects specific to a region or country.

COMPETITIVE ENVIRONMENT AND BANK MANAGEMENT

Evidence on the Conversion to a Single Model of the Banking Firm

It was anticipated that either country of origin (competitive factors), type of diversification move (growth opportunity pursued), strategic style (management approach), type of respondent (distribution by sector) or sampling year, would provide a statistically significant grouping of results. The sample of closed form responses was then partitioned accordingly while, in order to cope with different scales across the questionnaire when calculating ANOVA and correlation coefficients, response values were transformed into the ratio of observed value to the average of total class mean. Class means were defined as either overall means (total sample and average answer value) or the average value of the question when partitioned. It is noted that this transformation did not alter tests of significance in ANOVA or correlation results, which are shown in table 3 below.

Table III: Analysis of Variance (1996, 1999 and 2001)

(Class means included. Values sorted by individual respondents)

<i>Source of Variation</i>	<i>SS</i>	<i>Df</i>	<i>MS</i>	<i>F</i>	<i>P-value</i>	<i>F crit</i>
Between Groups	30.800	114	0.270	0.792	0.943	1.242
Within Groups	392.056	1150	0.340			
Total	422.857	1264				

Estimates of the One-way ANOVA supported the hypothesis of equal means when allowing indicators for country of origin and sample year, while failing to reject the null hypothesis of equal

means for any other grouping. These results would support the view that there is convergence on what might be described as a single model for a bank. In other words, provide evidence of a common view amongst bank managers (under the influence of the same competitive pressures) about the dynamics and control of the profit generating process.

At the same time, however, Spearman's Rank (linear) Correlation estimates failed to reject the null hypothesis of equal means. Estimates suggested that "country of origin" had a positive influence as an average correlation coefficient of 0.63 was recorded for the responses of Irish participants, 0.35 for British respondents and 0.30 for German respondents. Most of these coefficients were statistically significant when compared to the critical value ($r=0.305$, $p<0.05$). But only few correlation coefficients were statistically significant for Mexico in 1996 (0.13), Spain (0.11) or Mexico in 1999 (0.09). Furthermore and as noted by an anonymous referee, the fact that the survey commented on managers with direct responsibilities over 60% of the sum of total assets in individual markets and this was deemed sufficient to establish an agenda to research strategy formation in bank markets. Competitive factors, therefore, were considered to be more important for designing banks strategic planning frameworks than strategic management styles, type of diversification move pursued, the type of respondent (distribution by sector) or sampling year.

In summary, statistical tests suggested that the combination of great construct variety and sample size could result in no-one single dimension accruing for most of the variance in the results. But despite the data not being strong enough to achieve overall statistical significance, some results suggested partitioning the sample along the lines of "country of origin". The criteria to partition the sample emerged as correlation coefficients were not statistically significant when any other grouping divided the sample (not shown for brevity). At the same time, survey results did not unequivocally confirmed significant convergence on what might be described as a single model for a bank. But results did provide "soft" evidence of a common view amongst managers of banks (under the same competitive pressure) about the dynamics and control of the profit generating process. That is, evidence did emerge about the relationships between contextual elements and banks' corporate strategy. These results are discussed below.

Effects of Management Style over the Pursuit of Diversification

To establish the importance of anticipated advantage over diversification across bank markets interview results distinguished two distinct environments for the definition and implementation of

strategy. The divide reflected the mechanisms in place to discipline performance, with a clear separation between environments where strategic objectives received more emphasis and those in which budget returns were more important. It was expected that environments that favoured strategic objectives would be prone to greater diversification or to cross-subsidising activities. Moreover, the questionnaire provided a way to relate those environments to the management styles identified by Goold and Campbell (1987) and Goold *et al.* (1994).

During the course of the interview participants received a handout with a quote illustrating each of the management styles. Interviewees selected the style that best described their bank and also the style that best described bank management in their country. Afterwards, the interviewer requested a closed ("yes/no") answer to confirm the type of control, that is, the approach taken to the formulation of plans, strategies and budgets in the business process. According to Goold *et al.* (1994, p. 411), the type of control adopted by individual companies is identified by establishing whether top managers (or parent companies) are highly involved in the design of strategy, prefer to emphasise the achievement of financial targets or aim to balance these concerns. Table 4 offers the results, where Swedish and Estonian interviews were pooled together.

Table IV: Results of Strategic Style Selection (1996, 1999 and 2001)

(Percentages by country. Missing values excluded.)

	Strategic Style											
	1996				1999				2001			
	Mexico	Spain	UK	Average	Mexico	Ireland	Germany	Average	Sweden	Portugal	Average	
Financial Control	21.4%	13.0%	16.7%	17.0%	17.6%	27.3%	20.0%	21.6%	11.1%	7.7%	9.4%	
Strategic Control	35.7%	39.1%	22.2%	32.3%	35.3%	18.2%	10.0%	21.2%	22.2%	53.8%	38.0%	
Strategic Planning												
Type 1												
Centralised	0.0%	26.1%	44.4%	23.5%	11.8%	18.2%	40.0%	23.3%	44.4%	7.7%	26.1%	
Type 2												
Distributed	42.9%	21.7%	16.7%	27.1%	35.3%	36.4%	30.0%	33.9%	22.2%	30.8%	26.5%	
Sum	100.0%	100.0%	100.0%		100.0%	100.0%	100.0%		100.0%	100.0%		
	%	%	%		%	%						

Strategic Control was the prevailing style in 1996 and 2001 with respectively 32% and 38% of sample as expected by Goold *et al.* (1994, p. 414) but in 1999 the prevailing style was Distributed Strategic Planning (34%). Together Strategic Control and Distributed Strategic Planning accounted for 60% of the total sample suggesting that commercial bank management uses group inputs to identify strategic course of action. Only 17% of interviewees selected Financial Control in 1996 as their perceived management style and even with 22% in 1999 and 26% in 2001, it was the least common style of the sample. Cross-subsidisation, therefore, seems widely adopted as a standard of performance by established banks. The importance of cross-subsidisation was further supported by evidence emerging from Mexican markets where Centralised Strategic Planning was previously non-existent and then gained importance (to the demise of Distributed Strategic Planning and to a lesser extent Financial Control) as environmental turbulence subdued. Increased importance of Centralised Strategic Planning reflected how through the process of amalgamation of local players and acquisition of failed banks by foreign firms (see further Guillén and Tschoegl, 2000, pp. 13-16), Mexican banking organisations acquire competencies in the corporate centre. Trends in Mexican markets thus helped to corroborate previous findings suggesting strategic styles reflect (rather than cause) competitive advantage as well as confirm whether banking systems converge to a single model.

On balance, the cross-country distribution of survey results of 43% in 1996 and 35% in 1999 showed that in Mexico and in Ireland (36%) the most popular style was Distributed Strategic Planning. Strategic Control predominated in Spain (39%) and Portugal (54%), while Centralised Strategic Planning was most often selected in the UK (44%) and Germany (40%). These results would further suggest that competitive conditions could influence the selection of management styles at individual bank level.

The possibility that competitive conditions could influence the selection of management styles at individual bank level was sought by linking the geographic distribution of survey results to growth tendencies particular to each management style. The link emerged as the management styles of Goold and Campbell (1987) were based on research with British multinational companies. Later on Goold *et al.* (1993a,b) and Goold *et al.* (1994, p. 413) extended the original work to companies in all the main developed countries. However, a question that still remained unanswered was whether a markets' degree of competition influenced managers' basic beliefs regarding the relationship between financial targets, strategic targets and performance. The research project,

therefore, extended the work of Goold and Campbell (1987, p. 161) and Goold *et al.* (1994, p. 419) to consider growth tendencies particular to each management style in different competitive environments.

Table 5 offers the results of the form in which growth opportunities were identified by each management style at individual bank level. Results originated from the questionnaire requesting a closed ("yes/no") answer to confirm the role of business managers to identify diversification or market positioning moves.

Table V: Strategic Style and Role of Business Managers in Strategy Design, 1996

(Percentages by country. Missing values excluded.)

Strategic Style		Location of Growth Opportunities				
	Average	Mexico	Spain	UK	Average	
Financial Control	17.0%	<u>Mainly External</u> (Identify changing market conditions)				
		Agree	100.0%	100.0%	33.3%	77.8%
		Disagree	0.0%	0.0%	66.7%	22.2%
Strategic Control	32.3%	<u>Combination</u> (Changing market with core cap.)				
		Agree	100.0%	100.0%	100.0%	100.0%
		Disagree	0.0%	0.0%	0.0%	0.0%
Strategic Planning Type 1		<u>Mainly Internal</u> (Enhance core capabilities)				
		Agree	0.0%	66.7%	100.0%	55.6%
Centralised	23.5%	Disagree	0.0%	33.3%	0.0%	11.1%
Type 2		<u>Uncertain Growth</u> (Best strategy is adapting to change)				
		Agree	66.7%	100.0%	100.0%	88.9%
Distributed	27.1%	Disagree	33.3%	0.0%	0.0%	11.1%

In common with Goold *et al.* (1994, p. 418), survey results suggested that on balance growth tendencies particular to each management style bear a closer resemblance to the experience, philosophy and values of the management team than to the degree of competition in a market. In particular, results suggest that Centralised Strategic Planning banks favour organic growth, that is, for these banks excellence comes from enhancing core capabilities (56% on average). Alternatively, Distributed Strategic Planning banks could be run under managers' belief that no-one is able to determine growth opportunities with certainty and hence, excellence comes to those banks best prepared to adapt to change (89% on average).

Financial Control banks favoured diversification through acquisitions and considered that the best people to identify growth opportunities were business managers. This is so because managers of Financial Control banks believe that growth opportunities in bank markets are primarily determined by changes in market conditions (78% on average).

Strategic Control banks also favoured growth through core capabilities but balanced this growth with consolidation or divestiture of non-performing businesses. Managers of Strategic Control banks aim to maintain without change the overall dimension of the bank while, at the same time, aim to achieve a balance between market opportunities and enhanced core capabilities (100%).

In summary, results on management styles thus suggest that the overwhelming majority of banks use group inputs to determine strategic targets, overcome environmental turbulence or deter competitive threats. Bank managers seem more likely to adopt tactical moves for growth because of managers' belief that growth for banks is a result of high resource flexibility and thus, favour cross-subsidisation to provide stable financial results. Core competencies are perceived as a broad platform for growth and superior profitability is expected for those banks that achieve economies of scope through product, market and customer group diversification rather than cross-border growth.

The following section provides more insights into the relationship between core capabilities and bank growth.

The Quest for Synergy through Diversification

The questionnaire was in a position to further inquire on the rationale behind banks developing competitive advantage through greater diversification rather than banks concentrating in the development of core capabilities. For among others Channon (1988, p. 335) and Canals (1994, p. 41), the rationale behind bank diversification patterns is a response to product market penetration strategies and unforeseen benefits of certain IT innovations. However, interview results suggested that the banks' main goal was to tap into new sources of income. Table 6 provides the ranks in order of importance that interviewees gave to the elements that determine the speed and direction of banks' diversification patterns (for alternative listings see Hamel and Prahalad, 1994, p. 246 or Canals, 1997, p. 106). The ranking of diversification drivers in bank markets are shown in table 6 emerged as interviewees chose the two most important objectives that would determine future

diversification decisions. The questionnaire, therefore, proceeded through the assessment of banks' drivers of diversification.

The ranking offers the rationale behind bank diversification that was common to five competitive environments. This ranking built by collecting comparable data on changes in growth opportunities and disregarding local regulatory constraints. As a result of this data collection protocol, survey results corroborated sector-wide phenomena common to all bank markets as opposed to effects specific to a region or country. Table 6 shows that greater income growth (rank 1 both in 1996, 1999 and 2001), risk control (rank 2 in 1996, 4 in 1999 and 3 in 2001), and improved performance of distribution channels (rank 4 in 1996, 2 in 1999 and 3 in 2001) were the most important. Acquiring new technology (rank 5 in 1996, 5 in 1999 and 4 in 2001) and changing business focus (rank 5 in 1996, 5 in 1999 and 6 in 2001) were the least important. Indeed, the discussion of 1996 rankings with participants in the 1999 (and of 1999 ranking with 2001 participants) further suggested that new sources of income growth were based on expected income streams and in turn, potential income streams were related to a valuation of entry threats and opportunities. This is discussed further below.

[Take in Table VI here]

Results on diversification decisions corroborated the importance of enhancing core capabilities (rank 4 in 1996, 3 in 1999 and 4 in 2001) as a driver of diversification strategies in bank markets. Individual discussions of rankings with participants suggested that management of diversity does not seem to be time invariant (see further Bátiz-Lazo and Wood, 1999). In 70% of the cases interviewees agreed there had been changes in the framework in which banks' pursued synergy since the current trend in regulatory change started (while 29% said there had been no change and 1% were undecisive). As reference for that evaluation, the questionnaire used 1980 as starting position to coincide with the both the end of foreign exchange restrictions and the beginning of direct control of the money supply in the UK. However, 1990 was used as reference in Mexican and Estonian interviews as the previous decade had been one characterised by the nationalisation of the banking system.

Interviewees told of how banks created new synergies in the pursuit of greater growth and interviewees expected that changes in synergy creation should be reflected in banks' diversification

and market positioning moves. New synergies required new capabilities and participants from all countries agreed that the current wave of change in synergy creation had carried through greater emphasis on customer profitability (this in spite of most interviewees failing to provide an articulated account of how to achieve that profitability). All countries recorded a shift from a supply-oriented strategic stance to the development of skills to retain customers and even becoming a one-stop financial service institution for their customers. At the same time, sceptics of universal banking questioned whether banks had the organisational or IT capabilities to deliver all potential synergies.

There was a general agreement that first mover advantage will be quickly eroded in bank markets. Product or service leadership was not a feasible alternative because pro-active strategies (in the form of product or service innovation) are subject to replication. There was a tendency in all countries to observe innovation that follows a bundle of changes in regulation policy (in particular that previously limiting banks' business portfolio or geographic scope), increases in per capita income and contextual elements. Innovations seemed oriented to increase the diversity of supply and to withstand non-financial competitors rather than other incumbents.

In the following section the inquiry relates changes in diversification to a valuation of entry threats to determine the validity of the perception that of non-bank and non-finance intermediaries can effectively challenge bank markets.

External Drivers of Change in Financial Markets

Table 7 formalised what participants regarded as the most important external sources of change. Constructs emerged from a survey carried out in 1993 [¹] and sponsored by the European Commission, a survey that:

"...covered 400 of Europe's leading banks and capital market players. Panel experts were also assembled in Europe, North America and Asia Pacific." (Gardener, 1995, p. 2).

The survey assessed regulatory and competitive developments in Europe resulting from the beginning of the Single Market Programme in Financial Services (in January 1993). The aim of the survey was corroborating findings reported in the famous Cecchini study [²] around the importance of changes in regulation implemented across Europe and "describing overall gains sought from completing the European [financial services] market" (Gardener 1995, p. 1). The original ranks given by interviewees from the 1993 survey are included in table 7 (labelled *EU*), to suggest that

regulatory developments, competition from established providers and technological change were the most important external changes to come in European banking and financial markets (idem, pp. 2 and 3). The original ranking thus disregarded as important other external factors that could influence the banking environment. These other external factors could have included:

- social developments (i.e. ageing population, growth in purchasing power or better informed consumers),
- potential changes in the markets for human resources or in the skills of the labour pool,
- changes in the business cycle (i.e. more volatile interest rates, exchange rates or inflation),
- opportunities in new markets (i.e. reduce role of the State in pension provision, continued privatisation or the opening up of Central and Eastern Europe), or the
- effectiveness of planning schemes (to modify the boundaries of bank markets, that is, considered the effects of greater concentration, new organisational models such as virtual banking, multi-channel delivery systems, reduced cost structures, etc.)

In spite of the above mentioned short comings, during the interviews a handout presented the list of constructs emerging from the 1993 survey and prompted interviewees to re-rank them in order of importance. These results are summarised in table 7.

[Take in Table VII here]

Changes in ranking that showed greater homogeneity between original responses and interview results were those of UK (where the average absolute value of changes in ranking was 1, standard deviation of 1.70), Portuguese (avg. 2, sd. 1.78) and German (avg. 2, sd. 1.88) participants. The results from Irish (avg. 3, sd. 2.44), Mexican (avg. 4, sd. 1.79), Spanish (avg. 3, sd. 2.88) and Swedish (avg. 4, sd. 2.83) participants showed the greatest heterogeneity. Results thus suggest a relationship between environmental turbulence and the perception of potential external change. The more stable environments showed little opportunity for diversification strategies of out-of-market participants contesting bank markets. Interviewees thought competition from new entrants occurred during up-swings rather than randomly. This result emerged from trends within all countries and confirmed the importance of the stage in the economic cycle over perceptions of potential threats to survival (see further Batiz-Lazo and Wood, 1999). Interviewees expected greater threats and new competitors (from bank and non-finance participants alike) during periods of economic recovery

rather than in a recession. Interviewees anticipated that market-growth expectations and budget constraints would only allow non-bank participants to make strategic diversification investments after an economic recession.

Along side changes in ranking between surveys, table 7 also includes “innovations”, that is, unanticipated answers outlined by the structure of the interview (Robson, 1993, p. 233). These new constructs allowed the questionnaire to relate the effects of external threats to survival over core capabilities, diversification decisions and the scale of commercial banks. The result was that participants had a higher regard for mergers and acquisitions than for new incumbents to discipline market behaviour. Amalgamations suggested interviewees expected an orderly exit of excess capital from the UK (44%), Spain (25%), Germany (5%) and Mexico (5% in 1999 and non existent in 1996). Acquisitions were also perceived as an alternative way to build up core business but without increasing risk profiles. Some participants acknowledged a lack of capabilities in the businesses where they expected greater growth potential and acquisitions were therefore considered the preferred path to swiftly develop capabilities.

Another interesting result showed technological advances increasing in importance from rank 5 in 1993, to rank 3 in 1996 and top of the list in 1999 and 2001. This result reflected the fact that technological innovations have changed growth opportunities in bank markets and, in the context of diversification decisions, opened up new opportunities for greater scope of operation or for enhancing the internal operation of established participants. Information technology applications, therefore, were perceived as an important force in modifying competition in bank markets. However, as mentioned above, acquiring new technology had been ranked at the bottom of the two most important objectives that would determine future diversification decisions. This would suggest that while IT applications having been perceived IT as an external force of change in bank markets, while internal IT innovations that enhancing core capabilities through computer or telecommunications applications seems to play a secondary role in the design of bank corporate strategy. In other words, participants perceived little control over IT related innovations as they thought that technological change originates in a realm outside their control.

In summary interviewees implicitly recognised the superiority of potential competitors’ capabilities in some of the markets in which they wished to compete. Moreover, that successful regulation policy and innovative IT applications created not only new entrants but also effective threats of entry. Managers of banks have responded by increasing the scale of their operations and

have diversified product and service offerings. In fact survey results would suggest that as a response to greater contestability of bank markets, senior bank executives have emphasised actions to fend off diversification strategies of non-bank and non-finance participants into bank markets rather than investing in the disciplined (and risky) budgetary allocations associated with following a visionary course of action.

SUMMARY OF FINDINGS

This research aimed to fill the gap left by little systematic evidence concerning whether banks which engage in strategic planning outperform those that do not. Different banks could have forecast differently and therefore have different capabilities to compete. The research therefore assumed that the combination of anticipation and implementation is the source of sustainable competitive advantage. Accordingly, the research considered whether bank senior executives actively engaged in strategic planning to forecast the most profitable growth alternative for their banks and whether this growth relied on enhancing established capabilities to compete, creating new capabilities or divesting established capabilities (as market-based transactions or non-bank providers could be more efficient brokers of funds). Along side the evaluation of whether anticipated creation of capabilities to compete is the source of competitive advantage in bank markets, the research was able to provide evidence on whether commercial banks can consider their strategic planning function on the same basis than any other diversified company.

The research used grounded work by Goold and Campbell (1987) and Goold *et al.* (1994) as the point of departure to benchmark external parameters and indicators that link management practice and competitive advantage creation. The framework provided a basis from which to test whether visionary strategies predispose managers to integrate strategic and financial control of capabilities in order to develop a competitive edge or whether, on balance, organisational flexibility is the source of competitive advantage creation in bank markets.

Empirical support then emerged from in-depth interviews as well as from closed form responses to semi-structured interviews with senior managers with direct and indirect responsibilities in bank markets, and working within distinct competitive environments. Triangulating managers in different competitive environments and points in time was used as a method of identifying phenomena generic to bank markets rather than to specific countries or geographies.

The cross-country distribution of survey results showed that Strategic Planning was the most popular stereotypical management style in bank markets and Financial Control the least common. Strategic Planning style identified with both an authoritative chief executive (called “centralised”) or a group of top managers (called “distributed”) who integrate business activities around strategic targets (such as market share) and thus, cross-subsidies activities (i.e. high-financial return businesses finance low-return businesses while the latter achieves its strategic goals). Research results thus suggested that a management style where a central planner (or group) prescribes detailed rules for divisions, subsidiaries and departments predominates amongst participants in bank markets. Cross-subsidisation, therefore, seems widely adopted as a form of “parenting advantage” in banking. In some instances this style reflects organisations acquiring capabilities expected to enhance the working knowledge of core business. But at the same time, this style could reflect the risk of banking organisations holding back the development of new areas of business or, even worse, being steer to pursue inappropriate growth opportunities when senior managers (i.e. central planners) lack understanding of the opportunities opened up by technological change or regulatory developments. The potential costs of bureaucracy (both in money and lost opportunities) are thus the dangers associated with what seems to be the predominant management style in banking.

Indeed, research results suggest generic strategies such as unbridled diversification are perceived to have achieved partial success. Interview results suggested that regulatory policy created a perception that banks could safely grow disregarding non-bank competitors and with bank senior managers lacking a clear perception of their banks core capabilities, that is, with senior managers lacking control (or understanding) of profit generating resources. Interview results suggested the increasing importance of non-bank and non-finance intermediaries as potential challengers of bank markets are based on them having capabilities not yet developed by banks.

Results also suggested that competitive conditions could influence the selection of management styles at individual bank level. The possibility that competitive conditions could influence the selection of management styles at individual bank level was investigated by linking the geographic distribution of survey results to growth tendencies particular to each management style. The link emerged as the management styles of Goold and Campbell (1987) and Goold *et al.* (1994) were extended to consider whether a markets' degree of competition influenced managers' basic beliefs regarding the relationship between financial targets, strategic targets and performance. Survey results suggested that, on balance, growth tendencies particular to each management style bear a

closer resemblance to the experience, philosophy and values of the management team than to the degree of competition in a market.

The research then turned to assess whether anticipated advantage provides banks with access to a unique set of capabilities before or after regulatory and technological change. Establishing trends in the creation of capabilities to compete was important because as long as banks can preserve and develop their stock of unique capabilities then actual or new competition will be irrelevant to implement visionary strategies. Visionary strategies that enhance banks' core capabilities will, therefore, pre-empt competition from non-bank and non-finance intermediaries. Interview results suggested that only a reduced number of banks considered having access to a unique set of resources before or after regulatory change. Results suggested that the overwhelming majority of banks were likely to increase expected income streams by pursuing technological innovations and diversification (or market positioning moves) that have been already tried out (rather than developing their own capabilities). Interview results suggested a growing gap between bank growth and core capabilities which, in turn, reinforces the perception that non-finance intermediaries can easily contest bank markets. The perception emerged as changes in bank markets arising from regulatory change and IT innovation created opportunities for new synergies while, at the same time, banks were unable to match them with the existing set of capabilities or creating related or new capabilities (such as those associated with customer value creation). This finding reinforced the perception that regulatory and technological change created effective threats of entry from non-bank and non-finance intermediaries as they had relevant capabilities prior to deregulation or technological innovation. Survey results, therefore, suggest that for the immediate future most banks will continue to seek new opportunities by increasing the number of services already provided to their customers and developing IT-based applications for market segmentation. Only a selected number of banks will pursue geographic diversification.

In summary, this paper offers an agenda for researching planning methods in bank markets. Empirical evidence support suggested that in bank markets tactical strategies were more likely to anticipate competitive advantage than strategic intent. Banks also seemed willing to use established capacity and develop new or related capabilities in already tested diversification or market positioning moves instead of making firm budgetary commitments to implement visionary strategies. Results thus suggest that anticipated advantage was deemed greater when organisational flexibility effectively responded to environmental change (i.e. tactical strategies) than when bank managers

focused on enhancing core capabilities (i.e. visionary strategies). Result also suggested that banks are more likely to develop core capabilities as a platform for growth through amalgamations within national boundaries and to pursue strategic targets that promise economies of scope as the basis to anticipate competitive advantage.

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Table VI: Drivers for Diversification Strategies (1996, 1999 and 2001)

(Importance of factors driving diversification strategies)

	1996				1999				2001		
	Mexico	Spain	UK	Avr.	Mexico	Fre	Ger	Avr.	Swe	Port	Avr.
Greater income growth	1	2	1	1	1	1	1	1	1	1	1
Improving the performance of distribution channels	7	2	3	4	1	2	2	2	3	3	3
Risk control	2	1	4	2	1	5	7	4	4	2	3
Improving the performance of core capabilities	3	6	2	4	4	3	3	3	2	6	4
Acquiring new technology	3	6	7	5	5	5	6	5	4	4	4
Other	5	4	5	5	6	4	4	5	6	4	5
Changing business focus	5	4	5	5	6	5	5	5	6	6	6

Competitive Threats and Diversification in Mexican and European Bank Markets

Table VI: External Forces of Change in Financial Markets (1993, 1996, 1999 and 2001)

(Average rank per year. Missing values excluded)

Year	Country	Innovations*			EC regulatory developments	Competition between banks and non-banks.	Competition from foreign financial institutions.	Domestic regulatory development	Technological advances.	Taxation changes.	Competition from new entrants	Introduction of new products	Increase in influence of borrowers	Increase in influence of international investors	Increase in the cost of funds	Depressed asset values	Credit crunch	Non-EC international regulatory development
		USGAAP	Monetary Union	Consolidation														
1993	Europe				1	2	3	4	5	6	7	8	9	10	11	12	13	14
	Spain				2	13	4	7	3	5	1	8	10	5	12	11	8	14
	UK				1	2	3	9	4	14	11	5	7	8	11	5	10	13
	Ireland				2	1	5	7	3	7	6	7	10	12	3	12	11	14
	Germany				1	4	9	11	3	8	2	7	6	5	10	14	12	13
	Sweden				1	12	10	3	9	10	6	7	5	2	12	3	8	12
	Portugal				1	6	2	10	5	7	3	9	4	8	13	14	11	12
1996	Average				3	3	3	5	3	10	4	8	10	9	10	12	12	13
	Change				-2	-1	0	-1	2	-4	3	0	-1	1	1	0	1	1
	Mexico	20%			5	7	2	1	3	9	4	10	10	6	8	12	13	14
	Spain	36%	5%		1	2	5	7	3	6	4	7	11	10	9	14	12	13
	Change				1	11	-1	0	0	-1	-3	1	-1	-5	3	-3	-4	1
	UK		44%		2	1	3	7	4	14	5	6	8	10	12	9	11	13
	Change				-1	1	0	2	0	0	6	-1	-1	-2	-1	-4	-1	0
1999	Average				7	4	4	6	1	12	5	5	8	9	11	10	8	11
	Change				-4	-1	-1	-1	2	-2	-1	3	2	0	-1	2	4	2
	Mexico		5%		13	3	4	2	1	14	8	5	6	10	11	9	7	11
	Change				-8	4	-2	-1	2	-5	-4	5	4	-4	-3	3	6	3
	Ireland				6	2	5	7	1	14	3	4	9	12	11	10	8	12
	Change				-4	-1	0	0	2	-7	3	3	1	-8	2	3	2	2
	Germany		5%		1	7	3	10	2	9	4	6	10	5	10	10	8	10
	Change					-3	6	1	1	-1	-2	1	-4	0	0	4	4	3
2001	Average				2	4	3	9	2	8	6	6	11	9	13	12	10	14
	Change				5	0	1	-3	-1	4	-1	-1	-3	0	-2	-2	-2	-3
	Sweden				1	3	4	9	2	8	5	6	10	7	14	10	12	13
	Change				0	9	6	-6	7	2	1	1	-5	-5	-2	-7	-4	-1
	Portugal				3	4	1	9	2	7	6	5	11	10	12	13	7	14
	Change				-2	2	1	1	3	0	-3	4	-7	-2	1	1	4	-2

Survey question:

What are the forces for change most likely to affect the structure of financial markets in your country?

Where: 1 = Most important and 14 = Least important.

Source: Gardener (1995) and own estimates.

* = Percent of all interviews per year.

END NOTES

¹ Arthur Andersen and Andersen Consulting (1993), European Banking and Capital Markets: A Strategic Forecast, The Economist Intelligence Unit, London.

² Commission of the European Communities (1998a) "The economics of 1992", European Economy, No. 35 (March).

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