

DIVERSIFICATION STRATEGY AND PERFORMANCE: A CASE STUDY OF THE
KENYAN LIFE INSURANCE INDUSTRY "

BY

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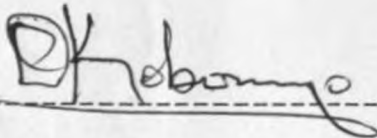
This project is my original work and has not been submitted for a degree in any other University

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This project has been submitted for examination with our approval as the university supervisors.

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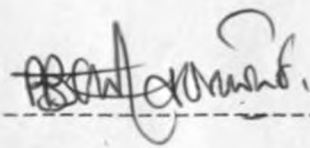
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ABSTRACT

This study was conducted with the objective of finding out whether highly diversified firms performed better than the less diversified firms.

The literature review defines the concept of diversification as used by various authors. The specific areas considered include the scope of diversification, dimensions of diversification and the rationale for diversification. The Kenyan insurance industry is also discussed including the kind of insurance business transacted in the Kenyan insurance market. In essence, the literature review develops a conceptualization of diversification in the insurance industry.

A questionnaire was used to collect primary data from the insurance firms. This data was used to classify the firms into the three diversity groups employed in the study. Secondary data was obtained from the Registrar General's Office and the Kenya Reinsurance Library. In particular, data was collected on the financial performance of the firms from the annual reports. A total of 10 firms out of 18 firms were included in the study. Analysis of variance was the main statistical tool used.

The findings of the study revealed that when the firms were classified on the basis of product diversification, the firms with medium diversity performed better than either the low or high diversity firms. When the firms were categorized on the basis of geographical diversification the firms that were highly diversified performed better than the two other groups. In both cases, the difference in performance was not statistically significant.

In spite of the limitations of this study, the findings may help to explain the weak but suggestive relationship found between the extent of diversification and performance, as measured by Return on Assets (ROA). This implies that performance is responsive to diversification.

... at the beginning of ...
... the business the firm is in or wants to be in.
... For small- and medium-sized firms, this business definition is usually
... which the firm's primary activities, the product or service category
... served by the firm, a category of large firms, and involved in
... multiple businesses; however, their business definition is more
... plain. But some organizations' activities are multiple and
... spread across a wide business the organization is currently in
... and in the affluence and affluence by which they achieve
... economic objectives of their growth strategy. A growth
... strategy is one that is aimed at increasing an organization's
... sales. A firm's growth strategy when

It increases the level of its activities higher than an
... organization of the next level into the future. For example, a
... significantly increases the market share of sales objectives.

It continues to serve the public in the same product/service
... market but adds new products/services.

It focuses its resources, activities on major functional per
... formance objectives.

It focuses its resources on one or more alternative growth
... strategies.

CHAPTER 1

INTRODUCTION

1.1 Background

The central factor examined at the beginning of strategy consideration is the business the firm is in or wants to be in. For smaller and medium firms, this business definition is simple enough: It merely describes the product or service category served by the firm. A majority of large firms are involved in multiple businesses; hence their business definition is more complex. But most organizations' strategic alternatives revolve around changes in the business the organization is currently in and in the efficiency and effectiveness by which they achieve corporate objectives in their chosen business sector. A growth strategy is one such strategic alternative an organization may pursue. A firm pursues growth strategy when:

- . It increases the level of its objectives higher than an extrapolation of the past level into the future. For example, it significantly increases its market share or sales objectives.
- . It continues to serve the public in the same product/service sector but adds new products/service sectors.
- . It focuses its strategic decisions on major functional performance increases.

Figure 1-1 summarizes the major alternative growth strategies available to a firm.

Figure 1-1
Growth strategies

-
1. Internal Growth
 - a. Single product/service or product/service line
 - b. Diversification
 - (1) Concentric/related diversification
 - (2) Conglomerate/unrelated diversification
 2. External growth (merger)
 - a. Single product/service or product/service line
 - b. Diversification
 - (1) Concentric/related diversification
 - (2) Conglomerate/unrelated diversification
 3. External growth (joint venture)
 4. Vertical integration.
-

Source: adapted from Glueck, W.F., Business Policy and Strategic Management, 1980, 3rd Ed. McGraw-Hill. pp 203.

Internal Growth: The first way in which a firm can grow is to increase the sales, profits, and market share of the current product/service line faster than it has been increasing them in the past. This can be done in several ways, for example, the firm can increase primary demand and encourage new uses for the product/service in the same area, with the same customers, pricing and products, and with the present organizational arrangement, or expand sales in additional sectors and geographic areas. The second way in which a firm can achieve internal growth is through diversification. This is a strategy in which the firm's objectives are achieved by adding products/services internally to the prior products/services. Concentric diversification takes place when the products/services added are similar to the present ones in one of several ways: technology, production, marketing channels, or customers. In a conglomerate diversification, the products/services are not significantly related to the present products/services in technology, production, marketing channels or customers.

External Growth: An external growth strategy is one in which the firm increases its level of objective achievement higher than an extrapolation of its past level by increasing sales and profits, by the purchase of product/service lines, namely, by mergers or joint ventures. A merger is a combination of two or more businesses in which one acquires assets and liabilities of the other in exchange for stock or cash or both companies are dissolved and assets and liabilities are combined and new stock is issued. A horizontal merger is a combination of two or more firms in the same business and aspects of the production process. In a concentric merger the firms combining are in businesses related by technology, production processes or markets. Whereas a conglomerate merger is a combination of firms in businesses which are not closely related by technology, production processes or markets. Joint ventures are formed when firms join together to achieve specific objectives.

Vertical Integration: This is a growth strategy characterized by the extension of the firm's business definition in two possible directions from the present. A backward integration involves a firm entering into the business of supplying some of its present inputs. Whereas forward integration moves the firm into the business of distributing the output of the firm by entering channels closer to the ultimate consumer.

Several reasons are given why firms may want to pursue a growth strategy. Some of these reasons are:

. In volatile industries, growth is necessary for the survival of the organization.

. Many executives equate growth to effectiveness.

. Some believe that society benefits from growth strategies.

. Managerial motivation. Growth strategies arise from power needs of many executives and these needs or drives encourage some executives to gamble and choose a grand strategy of growth. A growth company also becomes better known and may attract better management (Glueck, 1980).

. As firms grow in size and experience, they get better at what they do and reduce costs while improving productivity.

. Growth leads to effectiveness (as measured by profitability and other typical measures).

Of the growth strategies listed in figure 1, diversification is the most used strategy. This has led many researchers to pay more attention to it than the other growth strategies. In the sixties the center of interest was on conglomerate activity, (Berg, 1969; Gort, 1962; Turner, 1965). While in the seventies and eighties, the research has concentrated on the effects of diversification on performance of firms. According to McDougall and Round (1984) the justification of diversification as a corporate strategy appears to be based on three related themes. First, diversification has been related to profit maximizing behavior on the part of firms. It may enable a firm to obtain economic power and profits through, for example, predatory pricing behavior, the advantages of size per se, or the reduction of competition by removing potential rivals through mergers. It also may enable a firm to achieve higher profits through economies of scale, or through the exploitation of complementarities in production, distribution, marketing, research and development, purchasing, finance and management.

Second, a strategy of diversification can be linked to managerial theories of the firm. Diversification provides opportunities for growth in profits, sales and assets that are not possible through horizontal expansion. Third, diversification can be linked to risk reduction with the object of the firm being the reduction of relative or total risk associated with a firm's earnings and the exploitation of related benefits.

1.2 Statement of the Problem

In the recent past various statements have been made about the need for insurance firms to diversify. For example, the Vice President of Kenya Prof. George Saitoti advised the insurance firms to consider offering agriculture and livestock insurance services to farmers (Daily Nation, 16 November 1990). In response to this call, some insurance firms initiated the policy as part of their service package. The Commissioner of Insurance of Kenya, M.N. Muruthi, also called on insurance firms to expand life insurance business and venture into new lines such as medical insurance instead of competing for the few products available in the market (Nation 1990, 13 Dec.). And according to the chairman of Kenya National Assurance Company, the competition existing within the insurance industry, especially within the life business, calls for diversification. He asserts that his company is able to do well because it pursues diversification (Annual Report 1986). Further the presence of threats to core business and the presence of numerous opportunities, leads almost inevitably to consideration of a diversification strategy in order to strengthen the firm's revenue mix and finding new sources of

profitability. To justify these calls for insurance firms to diversify one needs to answer the question: Do diversified firms perform better than less diversified firms?

Some of the studies that have been carried out previously have given contradictory results. For example, Carter (1977) in a study of the performance of diversified firms, provided evidence which suggested that diversified firms out-performed their specialized counterparts (other things being equal) and that the source of the superior performance is the synergy that arises from diversification. Mcdougall and Round (1984) studied the motives for diversification and compared the performance of diversifying and non diversifying Australian industrial firms and found no significant difference in the profitability and risk faced by the two groups of companies. They however found that highly diversified firms were more profitable than the less diversified firms. In another study by Montgomery (1985) on market structure and performance, the results showed that diversified firms did not have higher market share in their respective markets than less diversified firms. In a later study, Montgomery and Wernerfelt (1988) reported that efficient diversifiers, which they defined as firms pursuing related types of diversification focusing on specific related skills, performed better than inefficient diversifiers when they competed in highly profitable industries. On the other hand, they found that inefficient diversifiers tended to prosper in less profitable environments. Furthermore, inefficient diversifiers were found to benefit more from markets with high growth than did efficient diversifiers.

Most of the studies have been done in the manufacturing sector as opposed to the service sector. The studies have also concentrated on measuring performance across industries as opposed to within industries. This could have affected the research findings in that firms from different industries experience different environmental constraints and opportunities which may have different influences on them. In addition, the service sector like the manufacturing sector, forms an important economic sector in any economy and its performance is important.

This study will attempt to provide an answer to the following question: Do highly diversified firms perform better than less diversified firms?

1.3 Objective of the Study

The major objective of this study is to find out whether highly diversified firms perform better than less diversified firms.

1.4 Significance of the Study

This study is of importance to managers who are involved in formulating corporate strategies. Since every manager aims at improving the performance of his organization, the findings of this study should help him in deciding whether to pursue a diversification strategy or not.

2.1 Scope of Diversification

2.1.1 Definition and Conceptual Framework

There are many ways in which diversification has been defined. Coddington and Moore (1987) defined diversification as a strategy that attempts to spread financial risk by taking advantage of new market opportunities. They point out in this definition that the concept of risk is important since it distinguishes diversification from vertical integration. Vertical integration is referred to as an attempt to control a major portion of a local or regional market by integrating backward or forward. According to these authors, vertical integration, just like diversification, is a way of achieving growth. An organization can either acquire its suppliers (backward integration) or acquire its distributors (forward integration). Some organizations do both. In diversification an organization moves into products or services that are clearly different from its current businesses.

Yet Ansoff (1957) in his paper, *Strategies for Diversification*, asserts that, one way to diversify, commonly known as vertical diversification, is to branch out into production of components, parts and material. This definition of diversification, at first glance, seems inconsistent with what we have just defined as diversification. However the difference is due to the fact that Ansoff looked at diversification from the point of view of the mission of the overall product, that the technology in fabrication and manufacture of these parts and materials is

likely to be very different from the technology of manufacturing the final product. Therefore according to him, vertical diversification does imply both catering to new missions and introduction of new products.

Bettis and Hall (1982) see diversification as a collection of businesses resulting from the fact that a firm competes in different industries. These industries have different structural characteristics (in the industrial organization sense), and these different structural characteristics result in different average profit in each industry. This definition is not different from that given by Gort (1966), that diversification is an increase in the number of industries in which a firm is active. This increase leads to a lower degree of specialization by the firm in its principal activity.

From these definitions, it is clear that, diversification involves a firm moving into new ventures from what it set out to do initially. It is important to note here that diversification may involve products, that is, introducing new products into the firm, serving different markets with the same products or different products; it may also involve moving out from one area of operation to other areas. This latter form is commonly referred to as geographical diversification.

2.1.2 Dimensions of Diversification

Every company defines, in one way or another, the business(es) it participates in. A first decision relates to the horizontal range of products: from specializing in a single product or a narrow segment of an industry, on one extreme, to

broad diversification into a wide variety of unrelated products on the other. Within the diversification option, different approaches are possible depending on the degree of "relatedness" of the various activities. The business units, each catering for a different product and market, may share commonalties in technology, production process, distribution, and customer base or the relatedness between the units may be virtually nonexistent.

Based on the relatedness of the businesses several dimensions of diversification can be discerned.

Kotler (1988) looks at diversification in a marketing perspective. He classifies diversification into three types;

1 Concentric diversification in which a company seeks new products that have technological and /or marketing synergies with existing product lines, even though the products may appeal to a new class of customers. This means the company goes into businesses which are related to the firm's current businesses.

2 Horizontal diversification in which the company searches for new products that could appeal to its current customers though technologically unrelated to its current product line.

3 Conglomerate diversification where the company takes on businesses that have no relationship to the company's current technology, products or markets.

Ansoff (1957) uses different classifications, which in content may not be very different from those of Kotler. They include;

1. Vertical diversification in which a company branches into the production of components, parts and materials. This classification may easily be confused with vertical integration. But Ansoff

hastens to add that the difference between vertical integration and vertical diversification lies in the mission to be served. In vertical diversification, components, parts and material are designed to perform certain missions, which are distinct from the mission of the overall product. Furthermore, he adds, the technology in fabrication and manufacture of these parts and materials are likely to be very different from the technology used in manufacturing the final product.

2. Horizontal diversification whereby new products are introduced which do not contribute to the present product line in any way, but cater for missions which lie within the company's know-how and experience in technology, finance and marketing.

3. Lateral diversification in which a company moves beyond the confines of the industry to which it belongs. This dimension of the strategy is similar to what Kotler describes as conglomerate diversification.

Simmonds (1990) looks at diversification from, the implementation point of view. He argues that the decision to diversify is part of a larger expansion decision by the firm, and includes the simultaneous consideration of both diversification breadth and mode.

Breadth refers to either related or unrelated diversification whereas mode refers to either internal or external diversification. Simmonds argues that, a firm deciding to diversify must make a choice of either related or unrelated diversification. That is, a firm may decide to seek new products that have technological and/or marketing synergies with existing product lines even though the products/services may appeal to a new class

of customers, in this case it will be considered as a related diversifier. Or a firm may decide to seek new products/services that have no relationship to the company's current product line in that case it is considered an unrelated diversifier. A concurrent decision is whether such diversification will be carried out through internal or external means. Internal diversification occurs when the current market share with current products is expanded whereas, external diversification occurs when a company decides to acquire or merge with another and absorbs it. These dimensions are summarized in Figure 2-1 below.

Figure 2-1: Dimensions of Diversification

Dimension	Internal	External
Relationship to Current Business	Related	Unrelated
Method of Acquisition	Organic	Acquisitive

Figure 2-2: Porter's Generic Strategies

Strategy	Focus	Scope
Cost Leadership	Price	Industry-wide
Cost Focus	Price	Targeted segments
Differentiation	Quality/Service	Industry-wide
Differentiation Focus	Quality/Service	Targeted segments
Focus on Cost	Price	Targeted segments
Focus on Differentiation	Quality/Service	Targeted segments

Figure 2-1 A Diversification Matrix

	INTERNAL MODE	EXTERNAL MODE
BREADTH		
<i>Horizontal Diversification</i>		
Market:		
Concentric/related	Develop products/services that serve similar customers in similar markets	Purchase products/services, companies that serve similar customers in similar markets.
Conglomerate/unrelated	Develop products/services that are different from present product line/markets.	purchase products/services, companies that serve different customers/market.
Technology:		
Concentric/related	Develop products that use technologies similar to present line.	Purchase firms which utilize technologies similar to present line.
Conglomerate/unrelated	Develop products that use technologies different from present line.	Purchase firm using technologies different from present line.
<i>Vertical Diversification (Vertical Integration)</i>		
Forward:		
Concentric/related	Develop outlets for sale of current products and related products to consumers	Purchase outlets for sale of products to customers.
Conglomerate/unrelated	Develop outlets for sale of different products to consumer.	
Backward:		
Concentric/related	Develop own supplier division to cover present materials	Purchase suppliers of raw materials.
Conglomerate/unrelated	develop own supplier division to cover different materials	

Source: Adapted from Glueck, W.F., Business Policy and Strategic Management, 3rd Ed. 1980, McGraw-Hill, pp 210.

2.1.3 Rationale for Diversification

There are many reasons why a firm might want to diversify. These may be dependent on the type of diversification strategy the organization wants to pursue. For example, Coddington and Moore (1987) identified seven major reasons a health care system might want to diversify:

1. Community service Address health care needs of the population that go un-met without hospital action.
2. Competitive positioning Maintain or improve the health system and medical center's competitive position.
3. Innovation operate at the cutting edge of new products, technology, and services in order to identify emerging new business opportunities.
4. Profit augmentation replace expected revenue and profit reductions in traditional areas (for example, inpatient service).
5. Risk management minimize overall organizational risk by spreading risks among a variety of ventures and markets.
6. Operating economies achieve operating economies (reduced costs) and improve utilization of existing resources (facilities, staff and so on).
7. Medical staff relations improve relationship with medical staff members, or augment their practices.

It should be noted that the initial reasons for establishing a new venture may not necessarily be the reasons for a business today. This is because in the initial stages, the reasons may not have been clearly defined but with passage of time, there may be significant changes in these reasons.

McDougall and Round (1984) assert that a general theory of diversification does not exist. Instead, the justification for such a corporate strategy appears to be based on three related themes first, diversification may be related to profit maximization behavior on the part of firms. It may enable a firm to obtain economic power and profits through, for example, predatory pricing behavior, the advantages of size per se, or the reduction of competition by removing potential rivals through conglomerate mergers. It also may enable a firm to achieve higher profits through economies of scale, or through the exploitation of complementarities in production, distribution, marketing, research and development, purchasing, finance and management. Second, a strategy of diversification can be linked to managerial theories of the firm. Diversification provides opportunities for growth in profits, sales, and assets that are not possible through horizontal expansion. Third, diversification can be linked to risk reduction, with the object of the firm being the reduction of relative or total risk associated with the firm's earnings stream and the exploitation of related benefits.

Michael Gort (Alberts and Segall, 1966) carried out research on firm diversification and expounded on the motives for diversification. He categorized these motives into five categories, which are discussed in the following paragraphs.

1. Diversification as a means of effecting economies of larger scale

This may be done by introducing new products or services to the firm or through mergers especially where the merging firms can operate more efficiently than they operated before. Diversifications through mergers accomplished by an exchange of stock with no new capital requirements make the basis for financing economies.

Administrative economies are other sources of possible gains that are associated with large firms. But it should be observed that from the standpoint of administrative efficiency, a diversification of this type leads to a serious diffusion of managerial time on operations that may not be vital to the firm's total earnings. In short, diversification can lead to a serious diversion of managerial effort from the problems that are really critical to the firm's success.

Research and Development economies can also be effected in that, a firm with a wide range of products has many opportunities for exploiting the results of a program of research. This is because the directions which research will produce results are to a large extent unpredictable. Consequently, the greater the range of activities, the higher the chances that a discovery of development in technology will fit into the firm's existing product structure. In the sense that economies are related not so much to size, in terms of output or investment as to the range of goods and services produced.

2. Diversification to use spare resources.

The simplest case of diversification rendered attractive by the presence of spare resources, involves by-products. This is especially true in manufacturing firms. Spare resources could also be in the form of spare capacity in managerial resources and in the sales force. Although instances in which spare resources are available for diversification are doubtless numerous, diversification often impinges on scarce resources.

3. Diversification to enter profitable industries

A very frequent rationale for diversification is to exploit a profitable opportunity in a sector or industry of the economy that promises a higher-than-average rate of return, especially where the objectives of the firm are long term. The critical factor in determining how profitable a venture will prove is the extent to which a firm has a competitive advantage relative to other potential entrants in the industry. In this connection, the traditional view has been that the competitive position of a firm in a new activity depends upon similarities in production techniques, raw materials and marketing operations between its old activities and the new one. The trend appears to be increasingly toward a different set of decisive relations between old and new activities, namely the skills and training required of managerial and technical personnel. Similarities in the required technical personnel skills are generally associated with similarities in production process but the two do not necessarily go together, nor are they usually present in the same degree.

Even in the absence of a powerful effect by diversification on rates of return, entry into new activities may exert an upward influence on stock prices. This might follow from exaggerated expectations by the investing public of the effects the new activities will have on overall earnings.

4 Diversification to Stabilize profits

One of the most frequently offered reason for diversification is the wish to stabilize earnings and sales, and there are two general contingencies against which stabilization may be desired. The first contingency may arise from the uncertainty of the environments that is, unforeseen, unique events such as permanent changes in consumer tastes, the other contingency is the business cycle.

There is a wide range of unforeseen events that affect sales revenues and earnings from particular products. Consequently, by increasing the number of industries or businesses in which it operates -through diversification- a company tends to reduce the chances of sharp declines in total company earnings that can arise from unpredictable changes in the economy. From the standpoint of cyclically stable industries, entry into an unstable industry may actually increase fluctuations in earnings. The two questions addressed when evaluating the effect of diversification on cyclical stability are; Is the new industry characterized by a relatively stable demand and (even if it is not) will the timing of peaks and troughs in the demand for the new products offset similar fluctuations for the older products? With respect to the second question, the more the the markets for

the new products are unlike those for the old products, the greater should be the contribution of diversification to cyclical stability. Against these advantage, one should note that, the risks of new ventures are higher when these ventures are in industries completely unlike those in which a firm's principal activities are located.

The risks against which it is really worth diversifying are those associated with long term consequences and those related to the instability of earnings. First, a sharp, tough, temporary decline in earnings may severely restrict a firm's financial resources and therefore limit its ability to exploit profitable investment opportunities. The firm may also be obliged to abandon highly profitable projects that do not have a rapid payoff. In extreme cases declines in earnings may even lead to bankruptcy. Second, a fluctuating income stream may have adverse effects on the expectations of investors with consequent negative influence on the price-earnings ratios for common stock. Diversification is often intended as protection against a permanent decline in earnings that could result from a fundamental change in the conditions of supply and demand.

5. Diversification for Growth

Another important rationale for diversification appears to be the desire for growth. A study by Gort (Ibid.) of diversification patterns showed that high-growth industries were entered far more frequently than those with modest rates of growth. Also low growth in the principle activities of firms tended to exert a positive influence on their attempts to diversify. In most in-

dustries, the rate of growth of market demand partially determines the extent to which a firm can grow. Even entry into relatively low-growth sectors of the economy will contribute to the rate at which a firm expands if the possibilities for expansion in its principal activities have been exhausted.

Growth as a factor in the personal motives of managers is fairly easy to understand. First, it carries prestige in the business community and elsewhere, second, the compensation of executives is generally related to the size of the firms they manage. But has the stockholder a stake in the rate at which a firm expands? The answer is fairly obvious if sales increases are for products with high profit rates; but to what extent can growth in itself, be an appropriate objective for the stockholder?

One reason for growth is that the morale of managerial personnel is, to some extent, related to the growth of the enterprise. Since opportunities for advancement are more limited in declining industries or firms, it is harder to recruit and retain people with high competence, and this, in turn, adversely affects corporate earnings prospects. In this sense an absolute decline or even a low growth rate can become a self reinforcing process that precipitates further declines or decelerations in growth. Needless to say, all the influences that affect growth breeds its own inefficiencies, which may offset the advantages noted above.

On the part of firms pursuing growth the advantage is that reinvestment of corporate earnings reduces the tax burden for stock holders whose income is subject to high marginal tax rates.

Growing industries are frequently selected because they are deemed to be most profitable. Although there is reason to expect growth to be associated with profitability, it is also true that industries tend to become more competitive as they grow, and this reduces their profitability in the long run.

It is important to note that a particular diversification strategy may be highly desirable for one of the objectives but less desirable for others. For example, if a firm shows declining volume of demand, it would be unwise to consider what Ansoff calls vertical diversification (1957), since this would be at least a temporary device to stave off an eventual decline of business. If a company shows every sign of healthy growth, then horizontal diversification would be a desirable device for strengthening the position of the company in a field in which its knowledge and experience are concentrated. If the major concern is stability under contingent forecasts, chances are that both horizontal and vertical diversification could not provide a sufficient stabilizing influence and that conglomerate action is called for.

In conclusion, the broader the market for a given product and the more complex the production process, the more specialization one would normally expect firms to be. And yet, notwithstanding the growth in markets and the increasing complexity of technology, the trend for companies seems to be toward greater diversification rather than toward specialization.

2.2 Research on Diversification

Research into the relationship between diversification and firm performance has yielded mixed results. For example, Carter (1977) in a study of the performance of diversified firms, provided evidence which suggested that diversified firms outperformed their specialized counterparts (other things being equal) and that the source of the superior performance is the synergy that arises from diversification. Mcdougall and Round (1984) studied the motives for diversification and compared the performance of diversifying and non diversifying Australian industrial firms and found no significant difference in the profitability and risk faced by the two groups of companies. They however found that highly diversified firms were more profitable than the less diversified firms.

In a study of diversification, market structure and performance, Montgomery (1985) found that diversified firms did not have higher market share in their respective markets than less diversified firms. In a later study, Montgomery and Wernerfelt (1988) reported that efficient diversifiers, which they defined as firms pursuing related types of diversification focusing on specific related skills, performed better than inefficient diversifiers when they competed in highly profitable industries. On the other hand, they found that inefficient diversifiers tended to prosper in less profitable environments. Furthermore, inefficient diversifiers were found to benefit more from markets with high growth than did efficient diversifiers.

Research findings on specific dimensions of diversification have also been contradictory. For example, Amit and Livnant (1988), Nguyen and Divenney (1990), Simmonds (1990) and Varadarajan and Ramanujam (1987) have shown that related diversifiers out-performed unrelated diversifiers. On the other hand, Bettis and Hall (1982), in a study of risk and return in a sample of related and unrelated diversified firms, found no performance difference between the two groups of firms. Dubofsky and Varadarajan (1987) examining the relationship between diversification strategies and performance, using both accounting and market measures of performance, found that accounting measures suggested that related diversifiers were better performers while market measures suggested that unrelated diversifiers were better performers. They concluded that, depending on the type of performance measure used - accounting or market based - different inferences about the relationship between diversification and a firms' performance are likely to be made.

2.3 The Kenyan Insurance Industry

2.3.1 Role of Insurance in Kenya

The insurance industry in Kenya has developed over the years to provide individuals and organizations with means of protection against financial losses arising from accidents.

Although insurance is basically a risk transfers mechanism, the special procedures and systems which have developed over the years in insurance law and practice, gives it more continuity and uniformity than other random transfer of risks. The financial services it offers to clients is aimed at giving them economic security.

The essence of insurance is the pooling or spreading of risk, a function which facilitates many institutions and individuals to pay small sums of money in the form of premiums into a central pool from which much larger payments will be made to the few in the group who require compensation as a result of loss.

Insurance firms are also financial institutions. They are guardians of huge sums of money contributed by policy holders. For them to accomplish their obligation to their clients, insurance firms invest these funds in productive enterprises such as real estate. As investors, insurance firms are among the largest sources of long-term development capital in any economy. In addition, the insurance firms, in the process of providing insurance covers, also inculcate the habit of saving in individuals. Such savings are essential for the individual who saves as well as to the economy.

The industry also provides employment opportunities. Directly, by employing people in the industry to carry out the normal insurance activities, such as selling policies, managerial activities, and indirectly, through the various investment projects initiated by the industry.

The insurance industry generates considerable funds from the operations of individual firms, in the form of corporate income and premium taxes for the government. The insurers undertake research into loss prevention and risk minimization which measures lead to the improvement in risks and ultimately a saving of resources within the country through minimization of wastage. Insurance is therefore, vital for the economic development of the country.

2.3.2 The Structure of Insurance Industry in Kenya

The insurance industry in miniature form is a reflection of the Kenyan economy both in terms of ownership and sophistication or lack of it. The industry in Kenya has not reached the level of growth or sophistication of markets in developed countries. Annual statistical survey published by Kenya Reinsurance, shows that we are still net importers of reinsurance services. A fact that has been decried by the Vice President, Prof. Saitoti (Kenya Times 1990, Nov. 17^{Outdated}). He also noted that there was a growing trend whereby much of Kenya's foreign exchange was being lost through unnecessary reinsurance overseas.

The incorporation of insurance companies as required by the Insurance Act (1984), has lessened the need for the exportation of all the insurance premiums written in the Kenyan market as was

the case before 1978, when the industry was composed of many branches of overseas insurance companies . The retention ratio of net premium to gross premiums, by December 1989, was still less than 50% (Insurance Focus 1989).

At present there is one re-insurance firm, the Kenya Reinsurance Corporation, 38 insurance companies out of which 19 transact life assurance business, 70 insurance brokers and 2,500 insurance agents. In spite of statutory requirements that all insurance companies be locally incorporated, a number of companies and bodies that control a large share of the available business are still controlled from outside. They include, Alico, Provincial, Lion of Kenya, Phoenix, Britak, to mention just a few.

The other sizable portion of the market is shared between emerging indigenous owned companies and a small but strongly founded Asian companies. In this category we have companies such as Corporate, United , Gateway, Gemina and Pan Africa Insurance.

Due to the competition that exist within the industry, the insurance companies sell essentially identical services. According to Mwangi (Insurance Focus 1989), most of the competition is the defensive type, which has taken the form of pricing of services, complementary services, real and unreal service differentiation and obstruction of competitor's operations. Today the market is such that only the largest firms can afford to appeal to all segments of the Kenyan market. This implies that the small insurers have to concentrate their sales efforts on selected geographic and industrial segments of the markets to use their limited resources effectively. Yet the trend for both small and large companies is toward diversification of their service lines.

Most insurers concur that competition in Kenya has become quite stiff in recent years because there are more and more companies chasing fewer business opportunities. For instance, there were fourteen insurance companies actively operating in Kenya in the early part of the decade of the 1970's as compared with 38 at the present day which has meant that the industry has experienced considerable expansion in the number of companies competing for the market over a relatively short period of time. The result has been that competition has intensified beyond that which can reasonably be regarded as beneficial for the health of the industry of for the insuring public.

A new company wishing to enter the market has to create for itself a portfolio of business. If there is not enough new business, it has to attack the existing business, resulting in the available market having to be shared by a greater number of companies. This, of course, exemplifies the difficulties which a small or medium sized local company would experience when attempting to start up as an insurer. The existing established insurance companies would then be forced to defend their share of the market, probably by reducing premiums, or by offering other added incentives to attract the insuring public. Another method is to give higher rates of commission to brokers and other intermediaries so as to generate more business in that way.

Apart from competition, another factor that affects the insurance business worth noting is the increasing claims' consciousness on the part of the public. This means that many claims are made some of which might not reach the desk of an insurance company. This problem is by no means peculiar to Kenya, it is far

more aggravated, with the increasing degree of sophistication, in some western countries, resulting in more ingenious frauds. However, the rate of increase of this type of occurrence in Kenya is a disturbing factor and adds to the difficulties faced by insurance companies, because of the very fast rate of expansion in all sectors of the economy.

2.3.3 Government Regulation

The government of Kenya, through the Insurance Act Cap 487, regulates the insurance industry in one way or another. Of importance to this study is the regulation on insurance investments and types of businesses the insurance companies are allowed to make. For instance, insurance companies are not free to make whatever investments they wish. Because bad investments would jeopardize insurer solvency, thus strict limitations are established on the types of investments an insurer may make. In particular the Kenyan law requires that an insurer carrying on long-term insurance business may invest in any of the following (appendix c gives a more detailed list);

- Government securities and bonds
- prescribed statutory bodies
- local authority securities
- mortgages on unencumbered immovable properties in Kenya
- debentures
- preference shares or ordinary shares of public companies whose shares are quoted on the Stock Exchange in Kenya
- loans on life assurance policies

- deposits in banks for financial institutions or any other prescribed investments.

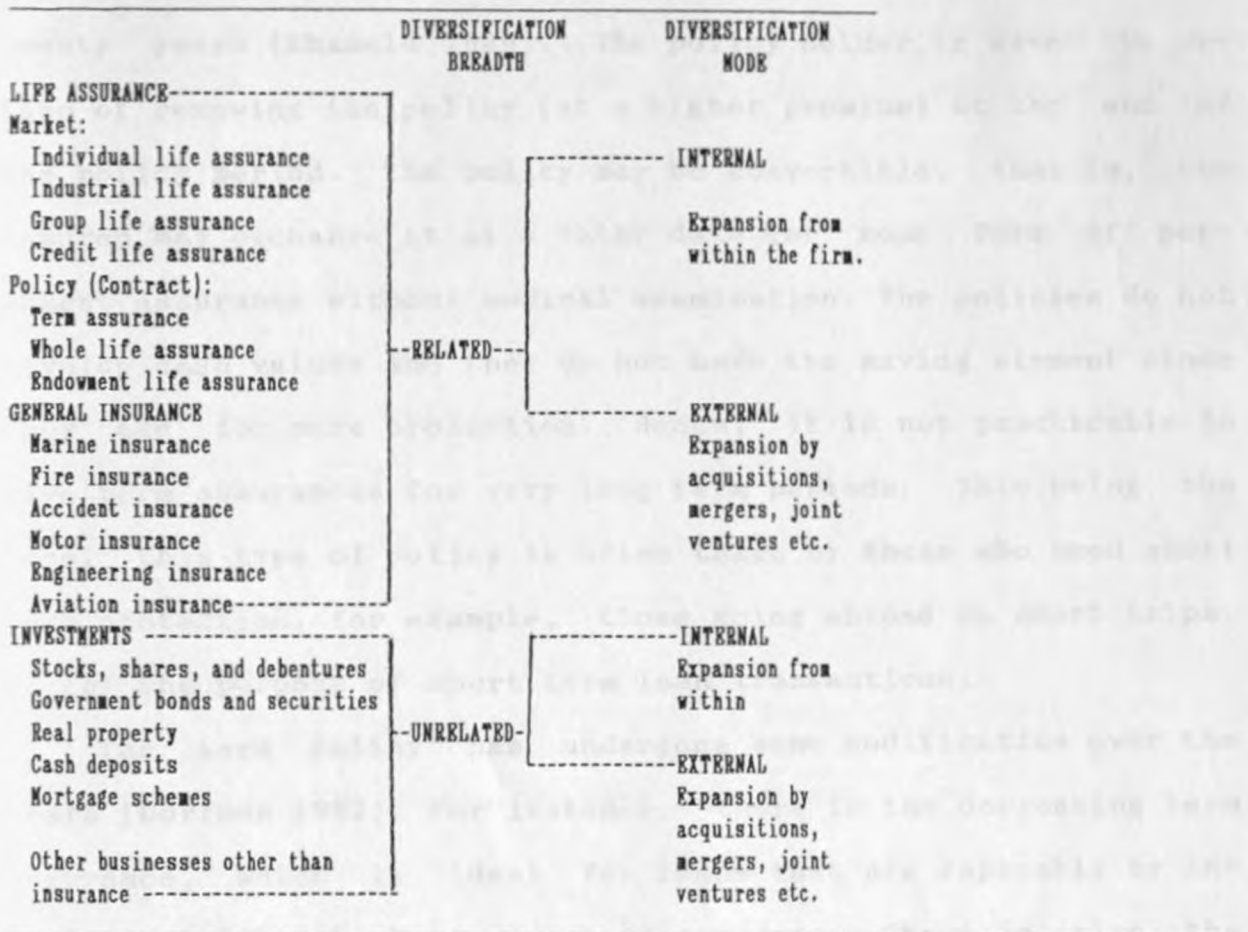
An insurer is also prohibited by the law not to directly or indirectly invest in a company, other than a bank or financial institution licensed under the banking act.

2.3.4 Conceptualization of Diversification in the Insurance Industry

Insurance services can be categorized into two broad classes, the first one is long-term or life assurance. The second, general insurance or non-life insurance. Long-Term insurance involves mainly life assurance on an individual or on a group basis. The pension or superannuation schemes are part of long-term insurance. General insurance normally involves covers for shorter durations of one or less years. The main headings under this classification are, aviation, engineering, fire, liability, marine, motor, personal accident and health, theft and workman's compensation insurances. These various classes of general insurance provide covers to meet varied needs of individuals and businesses.

A typical diversified insurance firm would be one that transacts all or most of the different insurance businesses shown in figure 2-2 and discussed in the succeeding pages.

Figure 2-2
A Classification of Insurance business and the related diversification dimensions.



2.3.5 Life Assurance

A great variety of policies are offered by life assurance firms. But there are three basic descriptions:

a) Term Assurance

These are the oldest form of policy, payment only being made by the assurer if the life assured dies within a specified period. It provides a temporary and cheap form of life cover. It is meant solely of the purposes of protection against the conse-

quences of death. This type of policies are usually without profits and are issued for terms ranging from a few weeks to twenty years (Khamala 1985). The policy holder is given the option of renewing the policy (at a higher premium) at the end of the policy period. The policy may be convertible, that is, the assured may exchange it at a later date for some form of permanent assurance without medical examination. The policies do not develop cash values and they do not have the saving element since they are for pure protection. Hence, it is not practicable to give term assurances for very long term periods. This being the case, this type of policy is often taken by those who need short term protection, for example, those going abroad on short trips, or for the purpose of short term loan transactions.

The term policy has undergone some modification over the years (Dorfman 1982). For instance, there is the decreasing term assurance, which is ideal for loans that are repayable by installments like the house purchase mortgage. There is also the increasing term policy which provides proceeds that increase each year. If death occurs in the first year of the policy, the face amount of the policy is paid. For example, suppose the face amount of the policy is Ksh 20,000; this is the amount that would be paid if the assured died in the first year of the policy. After 10 years, for example, perhaps Ksh 23,000 would be paid to the beneficiary.

b) Whole life assurance

Unlike term assurance which pays benefits only if death occurs during the term of the policy, whole life assurance provides protection for the whole of the assured's life time. These policies last for the whole of the assured's life, the sum being payable at death only. Premiums may be payable through out life, or cease at a given age, for example, 65 years. These policies are useful in providing against death duties, and for persons of normal health quite substantial benefits can be obtained for relatively low premiums. The distinguishing feature of this form of cover for the assurer is that the assurer knows for certain that eventually he must pay a claim on every whole life policy that is in force (Dorfman 1982).

Whole life policies can be broadly classified into three groups based on the method of premium payment.

(i) Single premium whole life policies; these are those in which the assurer promises to pay the sum assured, upon death, in exchange for one premium only, which is relatively large.

(ii) Continuous premium whole life (ordinary life policy) - the assured pays the same premium amounts (monthly, quarterly, semi-annually or annually) throughout his life.

(iii) Limited-payment life policies, these are variations of the ordinary life assurance in that, the sum assured is paid upon death but the premiums are limited to a fixed number of years, or until a certain stipulated age is attained. The shorter the period the larger the premium payment will be. The policy holder can arrange for the premiums to cease at the age when he expects

to retire from active business, so that when his income invariably falls on retirement, he will be in possession of a fully paid-up policy.

c) Endowment assurance

This policy has become very popular because the assured can benefit personally from the proceeds of the policy. The policy provides for the sum assured to be paid either at death, or after a fixed number of years, whichever comes first. This is a particularly suitable form of policy for the family man; in the event of his premature death, his dependents are provided for, if he survives the term, the policy moneys will be available for him to use as he wishes.

2.3.6 Variations in Life assurances

Variations and a number of adaptation of the basic forms are numerous, prompted both by the very competitive nature of this class of business and by the complex needs of society today.

1 Convertible term

This is a normal term assurance but with the valuable provision that the assured has the option to convert the policy into a whole life.

2 House Purchase

With more and more people borrowing money to buy their own houses, many schemes have been effected to give assistance, especially where the borrower dies before the loan has been repaid.

3 Assurances for children

a) child's deferred assurance

This policy is effected on the life of the parent for a selected number of years, terminating with an option date, when the child reaches a vesting age (usually 21). Until that time the premium is paid by the parent, but then the child has the option of having the assurance vested in his name and on his life, as a normal whole life or endowment policy, regardless of the child's medical condition.

b) Educational endowment

This is little more than an ordinary endowment policy, maturing by installments, to provide income to meet school and /or university fees.

c) Annuities

Strictly speaking annuities are not contracts of life assurance. They are a form of pension, whereby, in return for a certain sum of money (paid in a lumpsum ^{or} by installments), the assurer agrees to pay the annuitant an annual amount (annuity) for a specified period or for the remainder of the annuitants life. The annuity has its basic function the systematic liquidation of that which has been created, along either life assurance or non-life insurance lines such as savings bank accounts, stock or bond investments or real estate (Khamala 1982). Annuities may be classified using various bases. First, the annuity may be payable only for the duration of one or more lives. This covers single-life and joint-and-survivor annuities. Second, annuities may be categorized according to the time payments are to commence; an immediate annuity is one where the first payment is due

on one payment interval from the date of purchase. An annuity may also be deferred, that is, there is a spread of several years between the date of purchase and the beginning of the annuity payments.

Annuities may also be classified according to the method of premium payment, the annuity may be purchased by a single premium (the annuity to begin immediately or to be deferred) or it may be purchased in installments over a period of time. Another classification is on the basis of the nature of the assurer's obligation. A pure, single-life annuity provides payments for the balance of the annuitant's life time regardless of how long or short it may be. The obligation ceases upon the annuitant's death. Or the annuity may have a refund feature, with a specified amount to be paid to the annuitant's beneficiary should he die within a specified period after payments commence.

The above types of life assurances are typical of the Kenyan industry. But in recent years the industry is experiencing a proliferation of new covers, borrowed largely from the developed countries.

Life assurance has also been categorized into four main classes based on the manner in which they are marketed. These classes are: individual life, industrial life, group life and credit life.

2.3.7 Types of Life Assurance

Individual Life Assurance

Also called ordinary life assurance, this type of assurance describes the life policies purchased by individuals to fulfill their assurance needs. The premiums are paid either annually, semiannually, quarterly or monthly. The premiums are usually remitted using the "check-off" system in the case of employed assured, but they can also be paid by mail or in cash.

Industrial Life Assurance

This class is characterized by relatively small amounts of the premiums which are paid as frequently as once a week. Usually the premiums are collected by a representative from the assurer. It was designed to meet the needs of low-income workers. The small amounts of sums assured obtained from this class of assurance go towards meeting expenses such as funeral and burial expenses.

Group Life Assurance

This is life assurance provided to a well-defined group of people who are associated for some purpose other than purchasing life assurance. Common groups to whom this class of assurance is sold include employee groups and members of professional associations. Coverage is usually granted to the members of the group under one policy, called a master policy, without evidence of insurability, that is, without medical examination for the individual member of the group.

Credit Life Assurance

This life assurance is offered on both an individual and group basis. It is sold through lending institutions (like commercial banks, finance companies and hire purchase retailers) to short-term borrowers contemplating consumer purchases, and installment buyers. It also includes mortgage protection life assurance.

Credit life protects both the lenders and debtors against financial loss should the debtor die before completing the required payments. Plans available are usually written on term assurance basis, generally decreasing in amount as the loan is repaid over time. The life of the borrower is initially assured for an amount equal to the amount of the loan.

2.3.8 General Insurance

The major classes under this category include.

Marine insurance

This is the oldest type of insurance, it was practiced by the early Phoenician traders. Marine insurance covers perils arising from maritime trade and ventures. The various classes are;

- a) Hull - This relates to insurance of actual vessel and its machinery.
- b) Cargo - This relates to goods or merchandise carried by the ship.
- c) Freight - In maritime it refers to the cost of transporting goods, or hire of a vessel.
- d) Drilling rigs - Covers offshore installations.

Fire Insurance

The basic intention of the fire policy is to compensate for loss or damage caused by burning. To form a valid claim under the policy, there must be actual ignition which was accidental as far as the insured is concerned.

For additional premium, the standard fire policy may be extended to cover any of the following;

- a) bursting or overflowing of water tanks, apparatus or pipes.
- b) earthquakes
- c) explosions
- d) floods
- e) hail
- f) impact or damage by vehicles, animals, or articles from air, including aircraft.
- g) riot and /or civil commotion
- h) storm and tempest
- i) spontaneous combustion, self-heating or fermentation
- j) subsidence and landslide.

Accident Insurance

The term accident insurance is rather vague (Hansell 1989, 51), embracing what may be described as a miscellany of only slightly connected different classes of business. Hence, the exact constitution of an accident department will vary between insurers. The following comprise the major classes transacted under this category;

- a) fidelity guarantee (including contingency insurance)
- b) personal accident and sickness

- c) employers liability / *workmen's Compensation*
- d) public liability
- e) burglary or theft
- f) other types of insurance;
 - livestock
 - agriculture
 - glass, credit, rainfall, hail, licenses and so on.

An omission from the above list is motor insurance, this class has grown to such an extent that most insurers are regarding it as separate from their general accident portfolio.

Motor Insurance

There are a very wide variety of risks within the scope of motor insurance, due to the many different types of vehicles to be seen on the roads today. These risks, however, have been classified into the following categories;

- a) private cars
- b) motor cycles
- c) commercial vehicles (used for transporting goods or passengers for commercial purposes)
- d) agricultural and forestry vehicles
- e) special types (vehicles used for unusual construction or adaptation for example, moving cranes, ambulances, earth moving equipment)
- f) motor trade - individuals and firms operating within the motor trade.

For this category, except motor trade the policy available include;

- a) Act only - this is the minimum cover providing insurance cover sufficient only to comply with road traffic Act.
- b) Third party - covers the insured's legal liability towards the people arising out of the use of the vehicle
- c) Third party, fire and theft - it includes loss or damage arising from fires or theft only.
- d) comprehensive - it includes full third party cover, and virtually all accidental loss or damage to the insured vehicle.

Engineering Insurance

Includes the insurance of;

- a) boilers and other pressure vessels
- b) cranes, lifts, engines (steam, gas, or oil-powered)
- c) electrical plant (including refrigerators)
- d) computers
- e) miscellaneous equipment and machinery.

The covers provided for this category are divided into two;

- a) inspection services
- b) insurance cover

Aviation Insurance

Aviation insurance is a very specialized field. The main types of insurance available are;

- a) accidental damage to the aircraft itself
- b) liability for death, injury or property damage to third parties (not passengers)
- c) similar liabilities towards passenger
- d) cargo insurance

e) groups personnel accident insurance. Policies are arranged for aircraft crews and for travelers.

f) products liability, offered to aircraft manufacturers covering the liability arising from faulty design or manufacture.

Given the nature of their business, insurance firms, especially life assurance firms, are guardians of large sums of money contributed by policy holders. These funds must be invested in profitable ventures either on short term basis or on a long-term basis, depending on the circumstances of the company and the classes of business transacted. Life assurance funds are usually invested on a long-term basis and general business funds and reserves are invested on a short term basis so as to be readily available to meet unforeseen liabilities. Typical composite insurance company (transacting both life assurance and general insurance) would show the following in its investment portfolio (Irukwu 1984).

1. Stocks, shares, debentures of companies and commercial organizations. This may account for 30% of the company's portfolio.
2. Government bonds and other governmental guaranteed securities would comprise about 20%.
3. Mortgage loan - approximately 15% or more of the portfolio depending on a company's peculiar circumstances.
4. Real property (land, office blocks, warehouses and residential buildings) subject to the laws governing insurance company's investments in this class of property, 10% - 20%.
5. Cash deposits at banks at fixed interest rates and other miscellaneous investments may account for the remaining 15%.

An insurance firm may decide to transact life assurance business as well as general business in which case it pursues related diversification. Or the firm may decide to deal only in either life assurance or general insurance, in which case it is specialized in one area. Figure 2-2 summarizes the conceptualization of diversification within the insurance industry giving the classifications and the related diversification dimensions.

RESEARCH METHODOLOGY

3.1 Population

The population for this study consisted of all insurance firms registered to transact life insurance business in Kenya. A list of the companies was obtained from the Registrar General's Office and was updated by cross-checking with an insurance index appearing in the January issue of The Kenya Underwriter (see appendix B). The final list consisted of a total of 19 companies directly writing life assurance business. For the purpose of this study, a firm had to meet the following criteria to be considered relevant for the study:

- (1) It should have been in business before 1980 since the period of study was from 1980 to 1984.
- (2) It's annual reports were accessible as they provided data on financial performance.

Using the above criteria, 10 companies were found eligible for the study. All were used.

3.2 Data Collection

For each of the 10 firms in the study, the researcher compiled secondary data from the Registrar General's Office and the Kenya Reinsurance library. A lists of the firms, branches and subsidiaries was compiled for the period between 1980 - 1984. Financial data was collected from the annual reports (obtained from the Kenya Reinsurance Library). The data from the questionnaire (appendix A) was used to classify the firms into the various diversity groups. The Standard Industrial Classification

(SIC) codes could not be used since all the information needed to compile them was not available. For example, information on the individual activities of the firms was not available.

3.3 Measures of Variables.

3.3.1 Measures of Diversification

In a pioneering study of diversification and performance, Rumelt developed an approach to categorizing the extent and type of diversification of firms that is based on relatedness of products, markets and technologies (Varadarajan and Ramanujam, 1987). Subsequent research has been based on this categorization, some with a few modification, for example, Bettis and Hall (1982), Amit and Livnant (1988), Simmonds (1990).

Rumelt's classification has been, however, criticized by Varadarajan et.al. (1987), for being subjective and time consuming, involving assembling data from numerous fragmentary sources like annual reports, 10-Ks, and other publications. However, Montgomery (1982) had earlier demonstrated that the use of either Rumelt's approach or the traditional measures based on Standard Industrial Classification codes (SIC) produced similar classifications. Therefore extensions of Rumelt's work have simply circumvented the measurement problem by using the same firm and classifications he used (Bettis et. al. 1982; Montgomery, 1982; Dubofsky et. al. 1987; Barton, 1988).

Some researchers have attempted to develop measure of diversification that combine the conceptual attractiveness of Rumelt's scheme with the relative objectivity and accessibility of readily available data based on SIC codes (Montgomery, 1982; Varadarajan et.al. 1987; Simmonds, 1990).

Rumelt's classification is summarized in figure 3-1 below.

Figure 3-1
Rumelt's Classification System *

Specialization ratio **

95-100%	firms that are basically committed to a discrete business area	Single Business single business single vertical
70-94%	firms that have diversified to some extent but still obtain the preponderance of their revenues from a discrete business area	Dominant Business dominant vertical dominant constrained; dominant linked dominant unrelated
Less than 70%	Firms that are diversified and which more than 70% of the diversification has been accomplished by relating new activities to old	Related Business related constrained related linked
	firms that have diversified and in which less than 70% of the diversification is related to the firms original skills or strengths.	Unrelated Business multi-business unrelated portfolio

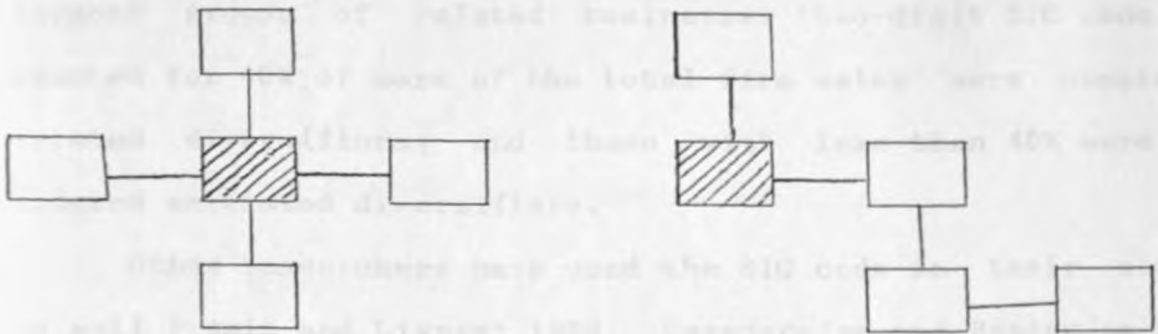
Notes

* From Montgomery (1982) pp 301

** Percentage of firm's total sales in a discrete business area.

! The distinction between constrained and linked diversification, a key point in Rumelt's methodology, is illustrated in figure 3-2.

Figure 3-2



Constrained pattern
(a)

Linked pattern
(b)

Assignment to a "main" diversification category is made on the basis of the percentage of a firm's total sales that can be attributed to a "discrete business area". Further differentiation is based on the pattern of linkages among a firm's business lines (figure 3-2). Pattern (a) represents a constrained diversifier wherein new endeavors are consistently related to one core organizational strength or characteristic. In contrast, the linked diversifier (b) has grown through relating new ventures to old, but not necessarily to one core strength or characteristic (Montgomery 1982).

The more traditional diversity measures have based on product count (product difference approach). It includes the use of Standard Industry Classification (SIC) codes. In this approach, business relatedness is generally captured through the use of ratios to measure the degree of business activity in a single business or group of business (Simmonds 1990). For example, in Simmonds' study each four-digit SIC code defined a unique business. All businesses with the same first two digits of the SIC code were deemed related, reflecting the classification

system's hierarchy of the two-digit as industries. Firms whose largest groups of related businesses (two-digit SIC code) accounted for 40% or more of the total firm sales were considered related diversifiers, and those with less than 40% were considered unrelated diversifiers.

Other researchers have used the SIC code in their studies as well (Amit and Livnant 1988; Varadarajan and Ramanujam 1987; Montgomery 1982). There is no agreement on which approach is superior to the other . Montgomery (1982) found that both Rumelt's categorization and the traditional approach produce similar classifications, but this was dismissed by Nathanson (1985). Thus, the measurement of diversification of firms remains a controversial and unsettled area. Nevertheless Varadarajan et al. (1987), re-examined the linkage between diversity and performance using a new method of categorizing firms based on their degree and direction of diversification. They state that the approach overcomes the problem of subjectivity inherent in Rumelt's classification scheme and makes no demands for detailed business level data that is a prerequisite of the Palepu's entropy measure (Varadarajan et al. 1987). They proposed a two-dimensional conceptualization of diversity in firms which distinguishes between two distinct patterns of diversification. The two patterns were from earlier works of Berry and Wood (Varadarajan et al. 1987), who used Narrow Spectrum diversification (NSD) and Broad Spectrum Diversification (BSD) as the dimensions. Varadarajan et al. modified this slightly and came up with what they called Mean Narrow Spectrum diversity, abbreviated as MNSD and Broad Spectrum Diversification or BSD. Figure 3-3 shows the resulting from cell

matrix, in which each cell represents the totality of a firm's past diversification activities in various two and four-digit SIC industry categories.

Figure 3-3: A two Dimensional Conceptualization of diversity in Firms.

Broad Spectrum Diversity*	High	Cell C: Unrelated diversified firms	Cell D: Firms with very high diversity
	Low	Cell A: Firms with very low diversity	Cell B: Related diversified firms
		Low	High

Mean Narrow Spectrum Diversity**

Source: Varadarajan et al, (1987) pp 383

Notes:

* Broad Spectrum Diversity (BSD) is the number of two-digit SIC categories in which a firm concurrently operates.

** Mean Narrow Spectrum Diversity (MNSD) is the number of four digit SIC categories in which a firm operates divided by the number of two-digit SIC categories in which it operates.

A desirable feature of this conceptualization is that it does not require data on revenues of business segments, but still provides insights into both (1) the degree of diversification (high versus low) and (2) its direction, predominantly related or predominantly unrelated. The firms are classified into the four cells of figure 3 using mean values of BSD and MNSD. For example, BSD (10.74, s.d.= 6.51) and MNSD (1.99, s.d.= 0.53).

Because this study could not meet most of the conditions required by the various methods described above, the researcher used a more subjective classification method. The responses from the questionnaire were used to classify the firms into the various diversity groups (appendix D). If a firm operated in less than 4 different insurance areas the firm was considered a low

diversifier. Those that operated between 5 - 7 different insurance areas were considered medium diversifiers and those that operated 8 and above different insurance areas were considered high diversifiers this captured product diversification. Geographical diversification was measured by the number of branches operated by each firm. Those with less than 5 branches, were considered low diversifiers, those with between 6 - 10 were considered medium diversifiers and those with 8 and above were considered high diversifiers. Subjective measures of diversity have been used before since controversy still exists as to which is the best method of measuring diversification (Simmonds 1991).

3.3.2 Measures of Performance

A common characteristic of past research on diversification is the use of accounting data to measure performance. Returns on Equity, Assets, Sales and Capital invested, have been frequently employed as they reflect a firm's performance over past years. Some researchers have however departed from this approach (Nguyen and Divenney 1990; Amit and Livnant 1988) and employed market-based measures of risk and return developed in the discipline of finance. Such measures are based on the price of a firm's stock, which conceptually reflects the market's perceptions of the firm's future performance. Other researchers have combined the accounting measures and market based measures to determine whether the results would differ (Dubofsky and Varadarajan 1987; Montgomery 1982; Varadarajan et al. 1987; Nguyen and Divenney 1990). The argument here is that, if the two measures measure performance, they should give similar results. Of the studies,

only the study by Dubofsky and Varadarajan gave conflicting results in that, they found different results for the different measures.

Return on Assets (ROA) is the most commonly used single accounting measure of performance (Simmonds 1990; Barton 1988; Bettis and Hall 1982; Hoskisson 1987; Varadarajan et al. 1987). The reason given for its wide usage is that return on assets reflects a return more directly under the control of management and is employed by managers, analysts and researchers. Further more, by contrast with return on equity, it controls for the effects of differing amounts of financial leverage. The other accounting measures suffer from the basic problems of accounting information and, in any case all are highly correlated (Bettis and Hall 1982).

Because of limited information on the market measures and to facilitate comparison of the results of this study with previous ones, the accounting data was used for measuring performance. Specifically, the return on assets measure was used since this information was available from the annual reports of the insurance firms surveyed.

3.4 Data Analysis

The simple analysis of variance was used to analyze the relationship between diversity and performance. Other researchers have used the same analysis tool in their studies (Varadarajan et.al 1987, Simmonds 1990, Bettis et.al. 1982).

CHAPTER 4

RESULTS, DISCUSSION AND CONCLUSION

The data in this study is summarized and presented by use of tables. Whereas percentages are used in most of these tables, the simple analysis of variance (ANOVA) test is used to make statistical inferences about the findings.

4.2 Findings

Tables 4-1, 4-2, and 4-3 summarize the types of products offered by the 10 insurance companies surveyed in this study. Table 4-4 gives the types of investments made by the companies.

(a) Long-Term Business

Each of the responding firms offered two or more of the various forms of life assurances available in Kenya today. As shown in Table 4-1, all the insurance companies transacted individual life assurance, 60% of the respondents transacted group life assurance, 50% credit life and pensions, 40% annuities and 20% handled industrial life assurance. Table 4-2, shows that 90% offer whole life policies, 70% endowment policies and 60% offer term assurances.

Table 4-1 Types of Insurance Offered by the Firms

	No. of Firms	Percentage
Market:		
Group life	6	60
Individual life	9	90
Industrial life	2	20
Credit life	5	50
Annuities	4	40
Pensions	5	50

Table 4-2 Types of Policies Offered by the Firms

	No. of Firms	Percentage
Policy (contract):		
Endowment policies	7	70
Term assurances	6	60
Whole life policies	9	90

(b) General Insurance

Table 4-3 summarizes the types of general insurance services offered by the firms surveyed. It indicates that all the 10 firms offer fire insurance, 90% handle personal accident, 80% offer engineering, marine, motor accident and workman's compensation insurances, 70% handle theft (burglary), 40% livestock and 30% handle aviation insurance. Others offer miscellaneous insurances such as agriculture and crop.

Table 4-3 Types of General Insurance Offered by the Firms

	No. of Firms	Percentage
Aviation	3	30
Engineering	8	80
Fire	10	100
Liability	8	80
Livestock	4	40
Marine	8	80
Motor	8	80
Motor Pool	9	90
Personal Accident	9	90
Theft	7	70
Workman's Compensation	8	70
Misc.	8	80

(c) Investments

All firms invest in government bonds and securities, mortgages and loans, real property and cash deposits, 90% have invested in ordinary shares both quoted and unquoted, 70% in local authority securities, 50% in preference share and 40% in debentures. This is summarized in Table 4-4.

Table 4-4 Types of Investments made by the Firms

	No. of Firms	percentage
Ordinary shares	9	90
Preference share	5	50
Debentures	4	40
Government Bonds and Securities	10	100
Local authority securities	7	70
Mortgages and loans	10	100
Real property	10	100

4.2.1 Diversification and Performance

The issue addressed by the study was whether there was a difference in performance between low diversifiers and highly diversified assurance companies. To be able to determine this issue, the firms were classified into three groups of low diversity, medium diversity and high diversity using two criteria; the extent of product diversification and the extent of geographical diversification. Table 4-5 presents the ranges of diversification for the bases used in the analysis. The first basis used to classify the firms, the average number of products offered by the firms, was calculated as shown in appendix D. Low diversity (range of 1-4) had a total number of 3 firms, Medium diversity (range of 5-7) had a total of 4 firms and the High diversity category (range of 8 and above) had a total of 3 firms. The geographical diversification basis was determined by the number of branches each firm had. In the first group, Low diversity, the range was 1-5 branches, had a total of 5 firms, Medium diversity, the range was 6-10, had a total of 3 firms and the High diversity group, those with over 11 branches, were 2.

Table 4-5 Classification of Firms by type of Diversification

Bases	Low		Medium		High	
	Range	No.	Range	No.	Range	No.
Product diversification	1-4	3	5-7	4	over 8	3
Geographical diversification	Below 5	5	6-10	3	over 11	2

In Table 4-6 the profitability of the three groups, low, medium and high diversity, is compared. The average rate of return are shown for the groups, for each of the bases of diversification and the differences are assessed using the analysis of variance test. The firms with medium diversity show better performance than the firms with low diversity and high diversity. Although the difference between medium group and the high group is smaller compared to the difference between medium and low groups. The firms with high geographical diversity showed better performance than either the low or medium geographic diversifiers. In neither case were the differences statistically significant.

Table 4-6 Average Rate of Return by Type of Diversification Group

	Diversification Groups		
	Low	Medium	High
Profitability Ratio;			
ROA (product diversity)	1.7	5.3	4.7
ROA (Geographic diversity)	4.7	2.1	6.0

Tables 4-7 and 4-8 summarize results of the analysis of variance test of the difference between performance of the various product diversification groups and geographical diversification groups respectively. The results show that there is no significant difference between the performance of the three groups. The obtained F value results in the failing to reject the null hypothesis. This means the probability that the three means (1.7, 5.3, and 4.7) differ merely by sampling error is high.

Therefore it is likely that the between groups variance estimate was not influenced by diversification. Similarly, when diversification groups are classified on the basis of geographic dispersion, the ANOVA test shows no significant difference in the performance of the three groups. This results are arrived at as shown in Table 4-8. Thus the analysis of the data reveals no significant differences in performance between insurance firms with low diversity, Medium diversity and High diversity, the basis underlying the formation of the groups makes no difference.

Table 4-7 A Summary Table of the ANOVA Analyses for the Effects of Product Diversification on Profitability.

SUMMARY TABLE

Source	df	SS	Ms	F ratio
Between groups	2	22.4	11.2	MS _{between} 11.2
Within groups	7	143.7	20.5	----- = ---- = 0.6
Total	9	166.1		MS _{within} 20.5

Critical Values (df = 2,7) *P_{0.05} = 4.74

**P_{0.01} = 9.55

F_{obs} < *F, i.e 0.6 < 4.74

Decision

Fail to reject H₀:

Table 4-7 A Summary Table of the ANOVA Analyses for the Effects of Geographic Diversification on Profitability.

Summary Table				
Source	df	SS	Ms	F ratio
Between groups	2	461.8	230.9	MS _{between} 230.9
Within groups	7	-294.7	-42.1	----- = ---- = -5.5
Total	9	166.1		MS _{within} -42.1

Critical Values (df = 2,7) *P_{0.05} = 4.74

**P_{0.01} = 9.55

F_{obs} < *F, i.e -5.5 < 4.74

Decision

Fail to reject H₀:

4.3 Discussion of Findings

The findings show that most of the insurance firms offer individual life assurance as opposed to industrial life assurance. The reason given for this by some of the respondents was that this type of assurance was most unprofitable due to the smallness of the market. The individual life assurance has been found to be more popular with the insuring public. With regard to the general business class, all the firms offered fire insurance and a majority offered personal accident. This is because these types of insurances are sought after by the public and in the long run are profitable to the insurance firms. Livestock Insurance is a relatively new service in the Kenyan insurance market. This could account for the fact that very few insurance firms offer it.

All the respondents invested in Government bonds and securities as well as in local authority securities. This is because the government requires that the insurance firms invest a certain percentage in these bonds and securities. On the other hand, the insurance firms actively invest in real property which includes residential as well as office buildings. This is due to the nature of insurance business, in that insurance firms hold large sums of money which may be used to finance viable projects such as property.

The results also showed that the insurance firms with medium diversity on average performed better than the high diversifiers and low diversifiers. Although the difference between the performance of high diversifiers was slightly lower than those of the medium diversifiers. The statistical analysis revealed that this

differences in performance between the three groups was not significant. These findings are consistent with some of the previous studies concerning the relationship between diversification and profitability as measured by the return on assets. McDougall and Round (1984), studied the motives for diversification and compared the performance of diversifying and non diversifying Australian industrial firms and found no significant difference in the profitability of the two groups of companies. They also used ROA as a measure of performance.

In this study, the lack of significant difference between the performance of the groups could be attributed to two major factors. The first was the relatively small number of firms that were used in the study. The second factor related to the conceptualization of diversification in the insurance industry. Due to the competition that exists within the industry, most of the firms have tended to offer basically the same products, the difference being in the brand names. This meant that there was no clear difference in the products offered by the different insurance firms.

In spite of these limitations the findings raise questions concerning the justification of a strategy of diversification and indicate some divergence between corporate motives for diversification and overall results. Clearly, these aspects require further research. Nevertheless, five general explanations may account for the results. First, the highly diversified firms may have placed greater emphasis on growth than on other performance parameters. Diversification may have been viewed as a means of overcoming the limitations of small markets with low growth rates

typical of the Kenyan insurance market (as explained in ch.2). Second, diversification expectations may not have been realized because of poor quality management and difficulties encountered in coping with new products and in capturing sufficient market share in markets which have specialized firms. Third, the costs of a strategy of diversification could have been greater than expected. Competition among the insurance firms for suitable diversification opportunities may have resulted in higher costs than were justified. In addition, inability to achieve expected scale economies, the existence of market imperfections, and government regulation (especially in respect of business and investment policy - see ch. 2) may have influenced the profitability effects of a policy of diversification.

Certain aspects of diversification, however, appear to have been favorable. The geographically diversified firms seemed to perform better than the less geographically diversified ones. The reason could be that due to the spread in branches the firms are able to capture a more wider market than their counter parts. The results in that respect, provide some tentative evidence that diversifying firms may perform better than the less diversified firms under more favorable economic conditions.

Fourthly, the fact that the insurance firms are limited by law to certain types of businesses and investments could explain the very fact that the industry pursues a related diversification strategy. Hence the difference in performance may not be well highlighted as would have been the case when unrelated diversification were pursued. In addition, past research has used firms from the manufacturing sector where differences in products

is easily determined. This study used insurance firms (service sector) in which a lot of competition has led to high product differentiation which is really not product diversification.

Fifth, the methodology employed in this study differed greatly from previous studies. Past researchers have frequently employed product count measures based on the Standard Industrial Classification (SIC) Codes because they are considered objective. In this study, the researcher used judgment and averages to assign the various firms into diversity groups. Thus, using different guidelines for assigning firms to groups could have influenced the results reported in this study. Further more, the size of the population was too small to capture the differences in performance between the groups. The researcher believes a larger sample would produce different results altogether. Future research should therefore be more focused on this dimension.

4.4 Conclusion

This study set out to determine whether highly diversified insurance firms performed better than the less diversified insurance firms. Three diversity groups were identified. The first were those firms with low diversity, that is, they offered few insurance products (1-4) to the market and operated below 5 branches. The second group, medium diversifiers offered several insurance products (5-7) and operated between 6-10 branches all over the country. The third category, high diversifiers offered over 8 of the insurance products found in the Kenyan market today and operated over 11 branches country wide.

Of particular interest was the finding that overall levels of diversification were not associated strongly with profitability. That is, product diversification produced results that the medium diversifiers appeared to outperform the firms with low diversity and high diversity. Yet the geographical diversification gave results to the effect that the high geographically diversified firms performed better than medium diversity firms and firms with low diversity. The results were not statistically significant.

Despite the shortcomings of the study, these findings may help to explain the weak but suggestive relationship found between extent of diversification and performance, as measured by ROA, to the extent that performance is responsive to the extent of diversification. It would be useful if future research would focus on more rigorous measures of diversification and use more measures of performance than were captured in this study.

4.5 Suggestions for Future Research

Due to the limitations discussed in the previous section, research could be carried out in this area, taking into consideration the various issues raised herein. For example, future research could be done using a longer time frame, a larger sample, define diversification using other parameters other than those used in this study, so as to bring out the relationship between diversification and performance more clearly.

More specifically future research should focus on;

(i) the multidimensional character of firm performance, and the relation between the market perception of managerial choice to diversify and accounting determined profitability (Amit and Livnant, 1988).

(ii) the integrated specification of managerial diversification strategies at the firm and industry levels, including the distinction between primary and secondary industries (Nguyen and Devinney 1990).

(iii) applications of modeling methods to capture the complexity of the diversification phenomenon as a dimension of industry structure (Bettis 1981).

4.6 Limitations of the Study

Two major limitations that have constrained the study and therefore the findings are; the extremely small population size and the lack of clear difference among the products offered by different insurance firms. The first limitation affected the statistical findings in that the small population used could not bring out the relationship between diversification and performance clearly. The second limitation affected the measurement of diversification in such a manner that most of the firms, although they may seem diversified, offer essentially the same kinds of products. This meant that the difference between diversification levels was not great.

Another limitation was that some firms were unwilling to provide the researcher with their annual reports and which were unavailable elsewhere this reduced the number of firms surveyed to 10 firms.

The results obtained in this study could have been influenced by the methodology used in assigning the firms into the three groups. Another methodology may result in the firms falling in different groups. The consequent differences results highlights the need for researchers to examine closely the composition of the groups they study for possible discrepancies.

Due to the above limitations the results of this study cannot be generalized.

APPENDIX A
QUESTIONNAIRE

Section A

1. What is the name of the company ?
2. When was the company established ?
3. Is the company; locally owned ()
 foreign owned ()
 parent company ()
 a subsidiary ()
 a joint venture ()
4. What is the total number of employees in the company ()

Section B

5. List the major classes of life assurance policies offered to your clients (under the headings provided)

Whole life assurance

Term assurance

Endowment life assurance

6. Which of the following type(s) of life assurance does your company deal in?

- () group life assurance
- () individual life assurance
- () industrial life assurance
- () credit life assurance
 (including mortgage protection)
- () pension schemes
- () annuities
- () others (specify)

7. Please list the major classes of general insurance transacted by the company in the space provided below.

8. If your company does not deal in some of the major types of assurance mentioned in (6) above. Tick all that apply.

- a. () the company deals with clients who do not need the assurances
- b. () the company is specializing in some assurances
- c. () it is the policy of the company not to deal in them
- d. () financial and other constraints make the company not deal in them.
- e. () it is not profitable to deal in them
- f. others (specify) _____

9. Please rank the reasons you have given above in order of importance. For example, 1. (e), would indicate that the reason (e) is the most important.

1 () 2 () 3 () 4 () 5 () 6 () 7 others (specify)

10. If your company deals in all of the major types of assurances mentioned in (6) above, what are some of the reasons you would give. Tick all that apply.

- () to achieve economies of scale
- () to use spare resources
- () to enter profitable industries, markets etc.
- () to stabilize profits
- () to pursue growth

Other reason(s) (specify) _____

Section C

11. How many subsidiaries does your company have? ()
If any, please list them below.

12. What activity(ies) do(es) the subsidiary(ies) engage in?
Please list them below.

13. What constitutes the company's investment portfolio. Tick all that apply.

- a. ordinary shares ()
- b. preference shares ()
- c. debentures ()
- d. government bonds and securities ()
- e. local authority securities ()
- f. mortgages and loans ()

- g. real property (including land, office blocks, residential buildings etc.) ()
- h. cash deposits ()
- i. Others (please specify)

THANK YOU FOR YOUR COOPERATION

APPENDIX B

A LIST OF LIFE ASSURANCE FIRMS

1. African International Insurance (ALL) ltd.
2. American Life Insurance Company
3. Appollo Insurance *
4. Blue Shield Assurance
5. British American Insurance *
6. Cannon Assurance
7. Co-operative Insurance Services *
8. Corporate Insurance
9. Fidelity Shield Insurance
10. Jubilee Insurance *
11. Kenindia Assurance *
12. Kenya National Assurance Company *
13. Insurance Company of East Africa *
14. Madison Insurance
15. Pan Africa Insurance *
16. Phoenix East Africa (Sun Alliance) *
17. Pioneer Insurance *
18. Stallion Insurance
19. Union Insurance

Note: * Those used in the study.

APPENDIX C

DETERMINATION OF ADMITTED ASSETS AND ADMITTED LIABILITIES FOR SOLVENCY PURPOSES

PART A

For the purposes of section 41 of the Act:

1. Assets shall be valued at values not exceeding their market or realizable value and in particular—

- (a) the value of lands and buildings shall not exceed the value determined on the basis of a valuation by a member of the Institute of Surveyors of Kenya who is not a permanent employee of the insurer, at least once in every five years or, at such shorter interval as the Commissioner may consider necessary, if the circumstance in any particular case so demand;
- (b) where the market value of any security, share, debenture, bond or other investment is not ascertainable, only such value, if any, shall be taken into account as is considered reasonable, having regard to the financial position of the issuing concern, the dividend paid by it during the preceding five years and other relevant factors;
- (c) the value of any computer equipment of an insurer,
 - (i) in the financial year of the insurer in which it is purchased, shall not exceed three-quarters of the cost thereof to the insurer;
 - (ii) in the first financial year thereafter, shall not be greater than one-half of that cost;

[Subsidiary]

(iii) in the second financial year thereafter, shall not be greater than one-quarter of that cost; and

(iv) in any subsequent financial year, shall be left out of the accounts;

(d) the value of office machinery (other than computer equipment), furniture, motor vehicles and other equipment shall be, in the financial year in which it is purchased, not greater than one-half of the cost thereof and shall be, in any subsequent financial year, left out of account;

(e) dead stock and stationery shall be excluded.

2. A proper value shall be placed on every item of the liabilities. In determining an insurer's liabilities, the share capital, general reserve, reserve for bad and doubtful debts, depreciation fund and other reserves of similar nature not created to meet specific liabilities approved by the Commissioner, shall be excluded. The liabilities listed hereafter shall be included to the extent indicated:

(a) Provision for dividends declared and outstanding, in full.

(b) Amounts due to other persons or bodies carrying on insurance business, in full.

(c) Amounts due to sundry creditors, in full.

(d) Provision for taxation, in full.

3. Adequate provisions shall be made, in accordance with methods approved by the Commissioner, in respect of unearned premiums, unexpired risks and outstanding claims, including provision for claims incurred but not reported.

4. Statements of admitted assets and admitted liabilities shall be prepared, separately in respect of—

(a) long-term insurance business; and

(b) general insurance business,

in the form prescribed in Part B of this Schedule.

Form No. INS. 41-1

All Amounts in Kenya Shillings

PART B

STATEMENT OF ADMITTED ASSETS AND ADMITTED LIABILITIES

Name of Insurer

As at 31st December, 19

Description	LONG-TERM INSURANCE BUSINESS		GENERAL INSURANCE BUSINESS	
	Market or Realizable Value	Book Value (as shown in balance sheet)	Market or Realizable Value	Book Value (as shown in balance sheet)
I. ADMITTED ASSETS				
(1) Investments Referred to Section 50(3) of the Act:				
(i) Kenya Government securities.				
(ii) Securities issued by statutory bodies prescribed under section 50(3) (b) of the Act.				
(iii) Securities issued by local authorities.				
(iv) Securities issued by organisations prescribed under section 50(3) (d) of the Act.				
Sub-Total (1)				

[Subsidiary]

FORM NO. INS. 41-1-(Contd.)

PART B

All Amounts in Kenya Shillings

STATEMENT OF ADMITTED ASSETS AND ADMITTED LIABILITIES

Name of Insurer

As at 31st December, 19

Description	LONG TERM INSURANCE BUSINESS		GENERAL INSURANCE BUSINESS	
	Market or Realisable Value	Book Value (as shown in balance sheet)	Market or Realisable Value	Book Value (as shown in balance sheet)
(2) Investments Referred to in Section 50(4) of the Act.				
(i) Mortgages on unencumbered immovable property in Kenya.				
(ii) Debentures secured by mortgage on unencumbered immovable property in Kenya.				
(iii) Loans on life assurance policies within their surrender values.				
(iv) Land and buildings in Kenya (i.e., instruments of title to immovable property in Kenya).				
(v) Debentures shares of public companies whose shares are quoted on stock exchange in Kenya.				
(vi) Preference shares of public companies whose shares are quoted on stock exchange in Kenya.				
(vii) Ordinary shares of public companies whose shares are quoted on stock exchange in Kenya.				
(viii) Deposits in banks or financial institutions licensed under the Banking Act.				
(ix) Other prescribed securities (specify).				
Sub-Total (2)				
(3) Other Admitted Assets				
(i) Debentures of public companies whose shares are not quoted on stock exchange in Kenya.				
(ii) Preference shares of companies whose shares are not quoted on Stock Exchange in Kenya.				
(iii) Ordinary shares of companies whose shares are not quoted on stock exchange in Kenya.				
(iv) Motor Vehicles.				
(v) Computer equipment.				
(vi) Office machinery (other than computer equipment), furniture, fixtures and other equipment.				
(vii) Premiums outstanding:				
(a) for not more than three months.				
(b) secured under automatic non-forfeiture conditions against the surrender values of life assurance policies.				
(viii) Amounts due from reinsurers.				
(ix) Amounts due from unrelated bodies.				
(x) Amounts due from related bodies engaged in insurance business.				
(xi) Interest, dividend and rents either outstanding or accrued but not due.				
(xii) Cash in hand and on current account in banks in Kenya.				
(xiii) Other assets* (specify).				
Sub-Total (3)				
TOTAL ADMITTED ASSETS (1+2+3)				

[Subsidiary]

FORM NO. INS. 41-1--(Contd.)

PART B

All Amounts in Kenya Shillings

STATEMENT OF ADMITTED ASSETS AND ADMITTED LIABILITIES

Name of Insurer

As at 31st December, 19

Description	LONG TERM INSURANCE BUSINESS		GENERAL INSURANCE BUSINESS	
	Market or Realisable Value	Book Value (as shown in balance sheet)	Market or Realisable Value	Book Value (as shown in balance sheet)
II OTHER ASSETS				
Assets which do not qualify as admitted assets: (i) On account of section 42 (1) of the Act. (ii) On account of Part A to this schedule.				
TOTAL OTHER ASSETS (i) + (ii)				
III. ADMITTED LIABILITIES	<i>Long Term Insurance Business</i>		<i>General Insurance Business</i>	
(1) Provisions— (i) Taxation. (ii) Dividends: declared and outstanding. (iii) Other provisions, excluding provision for doubtful debts. (2) Bank overdrafts and Bank loans. (3) Amounts due to related bodies excluding amounts shown under (4) below engaged— —insurance business; —other business (excluding banking). (4) Amounts due to insurers (including related bodies) under reinsurance contracts. (5) Other amounts due to insurers (not being related bodies). (6) Debentures. (7) Other loans: —secured; —unsecured. (8) Sundry creditors. (9) Other sums owing by the insurer (specify). (10) Underwriting provisions: (a) Estimated liability in respect of outstanding claims whether due or intimated. (b) Provision for incurred but not reported claims. (c) Annuities due and unpaid. (d) General insurance business Premium Provision:— —unearned premium provision. —other premium provision (specify). (e) Other underwriting provisions (specify). (f) Long term insurance business funds: Total amount standing to the credit of the statutory fund or funds maintained by the insurer in respect of long term insurance business or the amount of those liabilities as determined by an investigation performed in accordance with section 57 of the Act and approved by the Commissioner, whichever is the greater.				
TOTAL ADMITTED LIABILITIES				

Date:

Auditor

Principal Officer

APPENDIX D
MEASURES OF DIVERSIFICATION

Product Diversification

Respondent	Long-Term Business	General Business	Investments	Branches	Average
1	3	5	4	2	4
2	2	2	5	8	3
3	3	6	3	1	4
4	2	11	7	1	6.6
5	5	10	5	7	6.6
6	4	12	8	14	8
7	5	12	7	19	8
8	5	11	8	12	8
9	1	11	7	2	6
10	3	10	7	1	6.6

Diversity Groups:

Low Diversifiers average range, 1-4	(3 firms)
Medium Diversifiers average range, 5-7	(4 firms)
High Diversifiers average range, 8 and above	(3 firms)

Geographical diversification

Diversity Groups:

Low Diversifiers, No. of branches, Less than 5	(5 firms)
Medium Diversifiers, No. of branches, 6-10	(3 firms)
High Diversifiers, No. of branches, above 8	(2 firms)

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