PORTFOLIO HOLDINGS OF INSURANCE COMPANIES IN KENYA

by

THOMAS FREEMAN MEGBENU

A THESIS
SUBMITTED IN PARTIAL
FULFILMENT OF THE
REQUIREMENTS FOR THE
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MASTER OF BUSINESS ADMINISTRATION

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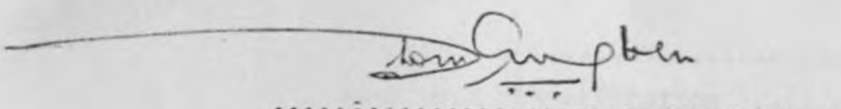
This Thesis is my Original Work and has not been presented for a degree in any other university.



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THOMAS FREEMAN MEGBENU
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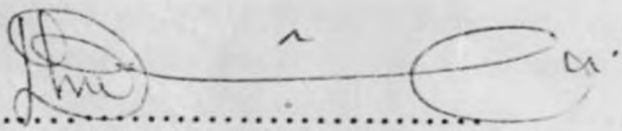
This Thesis has been submitted for examination with my approval as University Supervisor.



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DOUGLAS N. MUNGA
SUPERVISOR

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A C K N O W L E D G E M E N T S

Many individuals and organisations have contributed in many diverse ways in making this thesis what it is, and I do thank them sincerely for it.

I wish especially to thank Miss S. Shah and her staff at the Central Bureau of Statistics, who were very helpful in my data collection; D.N. Munga, whose useful comments and suggestions as my supervisor spurred me on all through; Mrs. S. Kabwegyere for her dedication and patience in typing the manuscript within limited time; and finally my wife, Abena, whose constant letters of moral and psychological encouragement kept me conscientious and alert to the end.

A B S T R A C T

The important role played by insurance companies as financial intermediaries cannot be under-estimated in a growing economy. As institutional investors in the capital market, they collect and administer savings on behalf of a large body of individual policyholders. In doing so insurance companies come between ultimate borrowers and ultimate lenders and thereby provide efficient allocation of available investible resources for development.

The purpose of this thesis is to study the portfolio holdings of insurance companies, both life and non-life, in the Kenyan economy during the period 1950 to 1974. Thus we are concerned with:

1. The extent to which changes in the port-folio holdings of insurance companies have reflected changing demands of the Kenyan economy.
2. What influences investment policies of insurance companies in Kenya.
3. The role of insurance companies with regard to government finance, the development of the capital market, the public and private sectors.
4. Whether insurance companies have a role to play in the developmental process.

In the light of the above objectives, it was found that:

1. Insurance fund managers are conservative investors who adopt a prudent image and pursue cautious portfolio policies because of their traditional concern for solvency.
2. Despite the large growth in their accumulated funds, insurance companies have responded only indirectly to the Kenyan situation by investing primarily in short-term assets and in other financial institutions and have had no appreciable impact on developing the already under-developed capital market.
3. Of late however, certain developments do suggest that the situation could be changed to make insurance companies increase their role in the economy without necessarily resorting to direct control of their operations.

With regard to methodology, the study relies heavily on analysis and interpretation of available published data on insurance business between 1950 and 1974 and supplemented by information collected through personal interviews with managers of insurance funds of a number of insurance companies.

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CHAPTER ONE

INTRODUCTION

The primary purpose of this introductory chapter is to provide the basis and groundwork upon which later chapters of this study will be developed. Section 1.1 attempts to review the growth and development of insurance business in Kenya and in East Africa as a whole and at the same time briefly gives the economic, financial and legal environment in which insurance companies operate in Kenya. More important in this section is a quantitative and qualitative analysis of insurance business during the pre-independence period (1950 to 1963) which will form the basis of evaluating the performance of insurance companies in the post-independence period in Chapters 2 and 3. For purposes of clarity, we find it necessary to discuss a general classification of insurance companies in section 1.2. Section 1.3 then takes up the question of insurance companies as financial intermediaries. The objectives of the whole study is stated in section 1.4. We close the chapter with the statement of hypotheses which we want to investigate in this study and the methodology employed.

1.1 General

The Kenyan economy has had a remarkably good run in terms of overall growth since the 1950s although not in terms of structural change, employment and income distribution. Gross Domestic Prooduct figures for 1954-1964 show that annual growth rate of 6 percent was recorded during the ten year

period. [1] However, the cost of living index rose at the rate of 2.5 per cent annually and this reduced the rate of growth of GDP to 3.5 per cent in real terms. At the same time the population was growing at the rate of 3 per cent per annum and this meant that real income per capita grew at the rate of only 0.5 per cent per annum. The monetary GDP, excluding subsistence or non-monetary activities, grew at the rate of 6.6 per cent per year and in real terms this amounted to an annual growth of 4.1 per cent. Thus real per capita monetary income grew by 1.1 per cent per year.

Agriculture which dominates the Kenyan economy made a contributuion of about 40 per cent per year to total GDP during the post-independence period. Manufacturing accounted for 9.4 per cent in 1956 and the share was still 9.4 per cent in 1963. Building and construction contributed 4.8 per cent in 1956 but the share fell to 1.9 in 1963. Commerce and other services contributed 23.3 per cent to total GDP in 1956 and the share had not changed much by 1963.

Growth rates during the post-independence period (1964 to 1972) also showed that GDP increased from K£330.1 million in 1964 to K£550.7 million in 1972 (at constant 1964 prices). [2] This represented a growth rate of 6.6 per cent per annum. Sectoral growth rates varied widely during this period, but most sectors of the economy achieved satisfactory growth rates. The fast growing sectors (annual growth rate per cent) were, Mining and Quarrying

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1. See Republic of Kenya, Development Plan, 1966-70 pp. 14
2. See Economic Survey, 1974, pp. 2

(11.5), Services (11.0), Building and Construction (10.8), Banking, Insurance and Real Estate (9.8), General Government (9.6), Manufacturing and Repairs (8.4), Forestry (7.4), Electricity and Water (7.3), Transport, Storage and Communications (6.8), Agriculture (6.0) and Wholesale and Retail Trade (5.5). All this represented a growth of 7.5 and 3.7 per cent per annum for the monetary and non-monetary sectors of the economy respectively.

The high rate of growth of the economy was stimulated by relatively high growth rates of investment and capital formation. Total capital formation in the economy grew at a rate of about 11 per cent annually between 1964 and 1973.[3] In 1974 however the growth rate of the GDP at constant prices was only 3.6 per cent as opposed to 6.5 per cent in 1973. The 1974 growth rate amounted to only a 0.2 per cent increase in per capita income. Thus, for the first time since independence, the relatively high growth of the economy was substantially reduced, and from then onwards the country began to face tougher economic conditions than before, as a result of difficult economic conditions.

The financial environment within which insurance companies operate in Kenya is characterized by the fact that a large part of the financial assets are held in the form of monetary deposits and quasi-monetary deposits, rather than in currency. The relatively high ratio of deposits to currency suggests that the banking habit is reasonably well developed. Dominating the

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3. See Economic Survey, 1975, pp. 13, 14.

financial system is the branch banking system which accounts for more than 65 per cent (See Table 1-1) of the estimated totals of deposits. Nevertheless, since the 1950's a considerable progress has been made in the development of other forms of financial intermediation. Thus the Kenya loanable funds market includes not only the banks but also a wide range of financial intermediaries. Private financial institutions have attracted a growing volume of private savings and they are quite well geared to the needs of the small saver by offering higher interest rates in some cases. A Stock Exchange has also been in existence since 1955.[4] By 1970 financial assets held in the financial system amounted to K£230.4 million. For the detailed analysis of the composition see Table 1-1 below:

TABLE 1-1

HOLDINGS OF SELECTED FINANCIAL ASSETS, 1970

	Amount (K£'000)	% of Total
Currency in Circulation	35,621	15.5
Commercial Bank Deposits:		
Demand	59,392	25.8
Savings	34,327	14.9
Time	26,577	11.5
Total: Banking System	155,917	67.7
Other Financial Assets:		
Post Office Savings Bank	5,334	2.3
Financial Institutions	11,992	5.2
Insurance Companies	33,734	14.6
National Social Security Fund	22,741	9.9
Government Debt (Held by Individuals)	719	0.3
Total	230,438	100.0

Source: Central Bank of Kenya: "Money and Banking in Kenya".

4. For detailed work on the Nairobi Stock Exchange, See D.N. Munga in unpublished MBA Thesis "The Nairobi Stock Exchange: Its History, Organization and Role in the Kenyan Economy", University of Nairobi, 1974.

It is clear from the table that among the financial intermediaries (excluding the banking system) insurance companies are the most important in quantitative terms.

Insurance business in Kenya is conducted under The Insurance Companies Act of 1965. Part IV, Section 16 (4) of the Act requires each company to conduct "its long term business in accordance with sound insurance principles". The Act also lays stress on solvency of companies to protect them against bankruptcies. Thus section 25 of the Act states that "an insurance company shall be deemed to possess the required margin of solvency if:

a) in the case of a company carrying on general business only, the value of its assets exceeds the amount of its liabilities by -

(i) fifty thousand pounds; or

(ii) one-tenth of the general premium income of company in its last preceding financial year, whichever is the greater amount;

b) in the case of a company carrying on a long term business only -

(i) its liabilities under unmatured life policies do not exceed the amount of its life assurance fund;

(ii) its liabilities under unmatured industrial policies do not exceed the amount of its industrial assurance fund".

These clauses are however applicable only after two years in business.

Before 1965 however, much of the law on insurance was designed to protect the African population. Under the "Control of the Business of Life Assurance with African Ordinance" 1945, in Kenya, elaborate procedures were instituted which effectively safeguarded the African from the security offered by life assurance.[5] Thus for instance, those wishing to undertake this business had to be approved by the Governor in Council, the Chief Native Commissioner was to approve all forms of proposals and policies, and no canvassing was allowed without the permission of the Provincial Commissioner. In Uganda four separate licenses were required to enable canvassing business throughout the whole country. As a result, in the early 1950's, the insurance companies and even the commercial banks, saw themselves as providing a service almost entirely to the expatriate community and had little interest in the more difficult African business.

Byamugisha [6] has pointed out, that insurance law in East Africa is nothing more than English insurance law. In the absence of a specific provision, the general law governing insurance is the law of contracts although insurance makes many exceptions. For instance, the insurance contracts may

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5. See J. Loxley, Makerere Institute of Social Research Conference Papers, January 1967, University of East Africa, (mimeo), "Financial Intermediaries and their Role in East Africa".

6. J. B. Byamugisha, "Insurance Law in East Africa," East African Literature Bureau, Nairobi, 1973.

be formed simply by the satisfaction of the offer, acceptance and consideration requirements. Again the Insurance Companies Act contemplates that an insurance contract will be in a policy and this "policy" may mean the contract or the document in which the contract is incorporated.

In theory, insurance companies do not go to people who are to be insured. Instead, the public are thought to go to the insruance company and ask it to insure them. The company may accept or refuse to insure. So the offer comes from the public and the acceptance comes from the company. In practice, however, the company issues its proposal form to the intending insured. After filling it in, the applicant leaves it to the company to study it before it accepts his offer. Such offer may be rejected and it will be rejected when the company thinks the would be insured, his subject-matter, or both are bad risks. When it is accepted, the company issues the policy containing all the terms of the insurance contract.

Policies give protection in respect of events occurring during the period of insurance. Anything happenning outside the period is not covered. Policies may be limited in duration by stated time or stated continued existence of a state of affairs. They expire at the end of the fixed period or at the ceasure of the state of affairs. For instance, a motor vehicle policy would normally run for one year, and many policies are on a yearly basis. But there are others such as the voyage or transit policies, in respect of which cover ceases after the voyage or transit. Life policies are on the same basis, they expire at the end of the life assured. This is not however

true of other types of insurance on life like health insurances, including accident which are time policies, usually running from year to year, and not determinable by the occurrence of the insured event.

Insurance companies transact much of their business through agents, many of whom are not their employees. There are some risks involved in this, to both the insurer and the insured, since the agents may not always be honest. In their efforts to win commissions, some insurance agents fail to live up to what is commendable. They push people into insurances without fully advising them of their rights and obligations; and from the cases which have come to the courts, it does not appear that they are always accurate in filling in the proposal forms for the many illiterates or non-English speaking applicants. [7]

Insurance is an aleatory contract. That is, recovery by the insured is conditional on the happenning of a specified event, which may or may not happen. The insured would in any case pay his premium to the insurer and would have to observe all the other terms of the insurance contract. As Byamugisha puts, it, "for a small sum (premium) the insured is assured of a much greater sum (indemnity) if a specific event occurs by which he is put to loss, damage or liability." An insured must first suffer actual loss before he is entitled to a share from the insurance pool. His entitlement will be only to the extent of the loss sustained, that is, no profits will accrue to the

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7. See J. B. Byamugisha, op. cit. p. 29.

insureds, and recovery will be subject to proof of actual loss and only to the extent of the loss.

Insurance is not strictly an investment. Profits are shared according to the amount invested. Although premiums are charged, but from each according to the risk to which the general pool is put because of the nature, quality and quantity of the subject matter for which the general pool is made a security. Premiums are fixed after taking into consideration a variety of factors. A fair estimate of losses ordinarily arising from the risk insured against is considered against the number of people desiring the insurance. The moral character and physical condition of the person applying for insurance may be as important as the physical quality of the subject matter desired to be insured. Thus "insurance companies will go into small details to elicit all necessary information, to impose all necessary protection and to indemnify for all necessary loss, so that the insurance pool is not depleted, and that some insureds do not subsidize others who could at times be snatching a windfall". [8]

The essence of insurance therefore lies in the elimination of the risk of loss for the individual through the combination of a large number of similarly exposed individuals who each contribute to a common fund premium payments sufficient to make good the loss caused to any one of them. It is the outstanding example of devices for dealing with uncertainty by consolidation.

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8. J. B. Byamugisha, op. cit. p. 38.

In practice only risks which in the long run are assessable over a wide field can be insured and they also have to be to some extent dependent on factors outside the control of insured individuals so that all participants have a chance, proportionate to their contributions, of benefitting from the fund. Again, since risks are not necessarily identical, they must be assessed before the contract is made to ensure that the contributions or premiums are a true reflection of the value of the right of each individual to benefit from the fund.

Having discussed the economic, financial and legal environment within which insurance companies have been operating in Kenya, we now turn our attention to a review of insurance business during the pre-independence period. Before doing so however, we must point out some limitations to the data available. Statistics on insurance business in East Africa were first collected in 1950 in respect of the years 1947 to 1949 and later covering up to the period 1957 which was published in 1958 by the East African Statistical Department. It was not until 1961 that the most up-to-date and revised figures for 1950 to 1958 were published. And even then these figures were consolidated for all the three East African states and including Zanzibar. Country-wise information and a few breakdowns only began to appear in the 1963 insurance statistics book.

Data therefore in respect of Kenya before 1963 are interpolations based on the assumption that during these years Kenya alone controlled over two-thirds of total financial assets.

One reason for this proposition is that the local head offices of most of the insurance companies in East Africa were in Nairobi. A breakdown of total financial assets for the three countries after 1963 also show that at all times the composition of Kenya was more than two-thirds. In 1964 for example, the total financial assets were £33.3 million and out of this £25.3 million were held in Kenya and the rest split evenly between Uganda and Tanzania. Dr. Loxley however, points out that this 75% of total local investment figure held in Kenya should not be seen from the point of view of net premiums, as only 55% of it originated in Kenya.[9] This he points out was because there had been a flow of insurance funds from Uganda and Tanzania to Kenya which was to be expected as the local head offices of most East African companies were in Nairobi. In view of these limitations, much of this review of insurance business until 1963 will be to some extent a review of insurance activities in the whole of the East African region.

By 1963, there were 121 insurance companies operating in East Africa and engaging in three categories of insurance, "life", "general insurance" and "life and general insurance". This figure represented an increase of 30 firms or 31.5% from 1950. During the fourteen year period the number of companies grew consistently until they reached a peak in 1956 when there were 136 firms. As Table 1-2 indicates both "life" and "life and general insurance" firms showed a steady increase until 1956 while "general insurance" showed slight falls during the last five years of the period after reaching a high figure of 99 firms

9. See J. Loxley, op. cit.

in 1960.

The sharp drop in the numbers of firms in life insurance in 1957 was due almost entirely to the Life Insurance Corporation of India taking over effective control of a large number of Indian firms.[10] Life insurance was nationalized in India in 1956 and the newly-created Life Insurance Corporation of India assumed operation of almost the entire life business of Indian insurance companies.

TABLE 1-2

NUMBER OF INSURANCE COMPANIES OPERATING IN EAST AFRICA, 1950-1963

YEAR	Life	General Insurance	Life and General Insurance	Total
1950	16	56	19	91
1951	16	63	22	101
1952	17	70	25	112
1953	17	67	25	109
1954	17	79	26	122
1955	18	83	29	130
1956	20	87	29	136
1957	10	93	20	123
1958	11	99	20	130
1959	14	98	18	130
1960	13	99	18	130
1961	12	97	19	128
1962	7	96	17	120
1963	10	96	15	121

Source: East African Insurance Statistics.

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10. See East African Insurance Statistics, 1950 - 1958

Thus the fall in the number of life insurance firms by half and in the number of life and general insurance firms by nearly a third indicates the very considerable Indian participation in the writing of life insurance in East Africa. Altogether some twenty firms were covered by the nationalization order. It must however be noted that this decline in the number of firms engaged in life business did not affect the amount of insurance premiums. The somewhat accelerated increase in the number of general insurance firms after 1956 was to some extent accounted for by the fact that those Indian companies which were engaged in life and general insurance business were after 1956 classified under general insurance. An important characteristic of the number of insurance companies registered in the East African territories during this period was the preponderance of foreign, particularly British, firms, a feature which as we shall see later is still dominant in insurance activities in Kenya. Table 1-3 shows the distribution of insurance companies by country of origin in 1958.

TABLE 1-3

INSURANCE COMPANIES BY COUNTRY OF ORIGIN, 1958

COUNTRY OF ORIGIN	NUMBER
United Kingdom	81
India	21
Union of South Africa	7
Kenya	6
Australia	6
Other countries	22

Source: East African Insurance Statistics

The growth in insurance business was reflected in the large increase in gross premiums direct during the period 1950 to 1963. Table 1-4 shows that gross premiums collected by insurance companies in Kenya rose from K£2 million in 1950 to K£8.3 million in 1963. Between 1950 and 1958 the percentage increase was 210% as compared with 28.2% between 1958 and 1963 while the overall growth during the 14-year period was 308.6%. Although gross claims direct went up during the period, this did not have any appreciable effect on net income which increased by K£2.5 million or 348.2%.

TABLE 1-4 K£'000

INCOME AND OUTGOINGS OF INSURANCE COMPANIES IN KENYA, 1950 - 1963

Year	Gross Premiums Direct	Total Income*	Gross Claims Direct	Total Claims**	Net Income
1950	2,021	2,080	721	1252	728
1958	6,393	6,752	2526	4439	2313
1963	8,301	9,397	3850	6133	3264

Source: Computed from E.A. Insurance Statistics, 1950 - 1963

* Includes interest, rents, fees etc.

** Includes expenses of management.

Various reasons accounted for the large increase in premiums during the period. Although developments in different classes of general insurance were also responsible, the growth of insurance premiums in life assurance was faster than in the other classes of insurance. The more rapid growth in life assurance was due to the growth of the non-African population coupled with very considerable increase of awareness of the benefits of life insurance by the African population. The main reason for the upward trend

in fire insurance premiums was the great postwar commercial development of the East African territories and the consequent increase in insurable interests. With respect to accident insurance, the increase in premiums was the result of the growing awareness by the public of hazards which may be covered by insurance as well as the substantial increase in the non-African population especially during the period 1950 to 1958. For example,non-African population rose by 74% from a level of 154,846 in 1948 to 290,327 in 1962. On the other hand, the major factor in the growth of employers' liability insurance was the legislation for workmens' compensation, increase in the labour force due to growing development, and the trend towards large scale employment (between 1958 and 1963 total number of people employed increased from 593,200 to 622,200). For motor vehicle insurance, a rapid growth of the number of motor vehicles on the roads plus the higher prices paid for them largely accounted for the increase in premiums. During the latter part of the 1950s especially due to losses incurred on motor vehicle insurance, insurers increased the rates for passenger cars which was also partly reflected in the rising premiums. Among all the classes of general insurance, marine insurance contributed to the slowest growth because of the tendency of exporters and importers to insure with companies abroad and partly because of a decrease in rates resulting from better port facilities.

Between 1950/1963 gross claims rose by K£3.1 million to K£3.8 million. Increasing expenses

of management were the major factors in this development. For reasons already given above, accident insurance revealed the highest increase in expenses of management followed by life insurance. One reason why expenses of management tend to be high for life insurance is that the number of new policies issued is large and high initial commissions are paid on new policies. It must also be pointed out that the very rapid growth in expenses of management was entirely consistent with the rapid growth of all classes of insurance in both Kenya and the East African region during this period. And from the national point of view this increase in expenses of management indicated growing contribution by insurance to national income primarily in the form of wages.

By 1963 investments of insurance companies in local assets amounted to K£21.4 million. The structure of their portfolio holdings showed that insurance companies were investing mainly in government and local government securities (34.1%) and 28.0% in mortgages and loans while 13.0% was held in real estate (see Table 1-5). Later in the following chapters we shall examine how far this structure of investment assets have changed since independence. It is also interesting to note that the bulk (84.4 %) of insurance portfolios (items 1 to 5) were in investments held primarily for income.

TABLE 1 - 5

ASSETS HELD BY INSURANCE COMPANIES IN KENYA, 1963

		Amount (K£'000)	% of Total
1.	Mortgages and Loans	6,013	28.0
2.	Government and Local Government Securities	7,325	34.1
3.	Treasury Bills and Development Bonds	-	-
4.	Stocks and Shares Including Debentures	2,002	9.3
5.	Real Estate	2,768	13.0
6.	Cash in Hand and at Bank	1,501	7.0
7.	Agents' Balances and Outstanding Premiums	1,069	5.1
8.	Other Assets	738	3.2
9.	Total	21,416	100.0

Source: East African Insurance Statistics.

1.2 Insurance Classification

It would be useful at this point to make a differentiation of various terms used to describe the kinds of insurance business so as to clarify the classification which we intend to adopt in this study. The main forms of insurance are listed in Table 1 - 6. Some of these categories cover wider risks than their actual title suggests; for example, fire insurance may embrace insurance against damages from civil disturbances, storms, earthquakes and other special risks. Life assurance is usually treated separately because it differs in many ways from the other categories which have many features in common with one another. Thus a common means of differentiation is to describe all forms of insurance other than life as "general" insurance. The characteristic feature of all forms of general insurance is that the contract is an annual one. The premium is paid in return for the promise of an indemnity if the specified contingency occurs during a given year; if there is a partial damage, an indemnity is paid to cover the actual loss.

TABLE 1-6

A CLASSIFICATION OF INSURANCE

A. Personal Insurance: Loss of income or increased expenditure through:

DEATH	SURVIVAL	ILL HEALTH	UNEMPLOYMENT
Life	Juvenile	Sickness	Unemployment
Burial	Old Age (Pensions)	Invalid	
		Accidental Injury	
		Maternity	

B. Property Insurance: Loss resulting from damage to, or destruction of property:

TANGIBLE PROPERTY	INTANGIBLE PROPERTY
Fire	Credit (Bad Debts)
Flood and Storm	Title and Mortgage
Marine	Corporate Bonding
Motor Vehicles	Business Interruption
Aircraft	Loss of Profits
Crop and Livestock	Market Loss
Property Depreciation	Strikes
Embezzlement	Compensation
Forgery	Public Liability
Burglary	Employers Liability
Theft	Reinsurance
Plate Glass	
Boiler	
Radiation	

Source: Derived from George Clayton and W.T. Osborn, "Insurance Company Investment, Principles and Policy".

Publisher?

The contract in life assurance differs from the contract in general because it is usually a long-term one and the premiums are paid over a number of years. In theory it is feasible to provide life cover on an annual basis but there are serious disadvantages in practice. Since most life assurances are effected f for the purpose of family protection in the event of death or to make provision for old age, a policy which terminates each year would be quite inadequate. A family man for instance needs a permanent contract at a reasonable premium which he knows in advance and for which he can provide in his annual budget. And a second important difference is that those who take out a long-term life assurance policy expect to make a claim on the insurance company because the event on the occurrence of which the claim is paid, e.g. death or the attainment of a given age, is certain to happen. The uncertainty arises from lack of knowledge as to when death will occur. On the other hand, in general insurance, the specified contingency - loss at sea or fire, for instance - may never happen to the individual policy-holders. It is this distinction which is the basis for using 'assurance' when describing the various types of life business and 'insurance' for general business.

Another classification which is more common in the U.S.A. is to refer to general insurance as 'fire and casualty' insurance or 'property and liability' insurance. A third way of differentiating insurance business is again to call all insurance other than life, 'non-life'. In this study, and for purposes of simplicity we shall adopt this last classification. From Table 1-2, we had noticed earlier that during the period under review, there

were three ways of classifying types of insurance in this country - 'life', 'general insurance', and 'life and general insurance'.

1.3 Insurance Companies as Financial Intermediaries

Financial intermediaries play a very important role in a developing economy. As the economy grows, this growth tends to be characterized by the the existence of increased financial intermediaries whose function is to channel flow of savings from ultimate savers to ultimate users, through indirect securities, either for investment in real assets or for consumption. These intermediaries purchase primary securities and in turn, issue their own securities. In doing so, they come between ultimate borrowers and ultimate lenders. In essence, they transform these primary securities (direct claims) into indirect securities (indirect claims). A life assurance company for example purchases mortgages and bonds and issues life assurance policies. Financial intermediaries do thus transform funds in such a way as to make them more attractive [11] by providing a variety of services such as economies of scale, divisibility and flexibility, diversification and risk, maturity, and expertise and convenience. [12] The existence of financial intermediaries therefore tends to make financial markets more efficient. By transforming primary securities into indirect securities, they lower the cost to the ultimate borrower and provide a security better suited to the ultimate lender. [13]

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11. See Rayomond Goldsmith, "Financial Institutions", New York, Random House, Inc., 1968, pp. 22, 23.

12. See James C. Van Horne, "Function and Analysis of Capital Market Rates", Prentice Hall, Inc., 1970, pp. 3 - 14.

13. Ibid, Chapter 2.

The importance of insurance companies as institutional investors is derived from their function as intermediaries in the capital market who collect and administer savings on behalf of a large body of individual policyholders. As such forms of savings continue to grow, (not only through insurance companies but through the other non-bank financial intermediaries) the investment activities of the institutions accepting them have more and more impact on official policy and exert greater influence over the amount and type of securities offered in the capital market. The activities of these financial intermediaries do have theoretical and practical implications. They may for instance make net additions to the supply of loanable funds available to deficit units (units whose planned expenditures are in excess of funds arising out of the current income flow) by mobilizing the public's idle balances through sales of securities out of their existing portfolios. Again, on a practical level their decisions about the population of their current funds which they are prepared to place at the disposal of the public sector are of great significance for the operation of monetary policy and debt management. Their size, as for instance in Britain and the U.S.A., gives them great power in directing the flow of capital and their relative preferences for the various forms of private debt and for the obligations of different types and sizes of company, has a qualitative effect on capital formation.

Until recently traditional monetary theory treated as neutral the effects of non-bank financial intermediaries such as building societies, hire-purchase finance companies, industrial banks and

insurance companies on monetary demand. This was because developments in monetary theory evolved from the analysis of a world dominated by commercial banks whose liabilities are widely accepted as money. And secondly, that only commercial banks have the power to create money. Pre-Keynesian and Keynesian models therefore had practically no room for the investment behaviour of savings institutions, since investment decisions were assumed to be made by individuals. And again that, the only current flow of funds in the system is that which originates in the banks, and their obligations were assumed to shape the choice open to potential investors. However it is now known that the market for loanable funds in the modern capital market is influenced more by investment decisions made by portfolio managers in financial institutions and less by individuals trading on their own account. This is because the motivations which guide such institutional investors are different from those of private individuals. For instance, Clayton and Osborn point out that the emergence of large-scale non-bank financial institutions, such as insurance companies, in money and capital markets has greatly altered the conditions under which the price of credit is fixed. [14]

Although there is evidence about insurance companies that the contractual nature of funds which flow through them confirms the view that they are channelling current savings into the capital market, they can also contribute to monetary instability. If for instance, at various times they accumulate idle balances in accordance with Keynes's speculative motive, they can act as agents in the process

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14. See George Clayton and W. T. Osborn, "Insurance Company Investment, Principles and Policy", George Allen & Unwin Ltd., London, 1965, Chapter 2. page 7

whereby savings are caught in the liquidity trap and are not transmitted through the market to finance capital formation. Thus it becomes important to study their attitude to liquidity and to see how far their holdings of cash and other portfolios have varied through time owing to uncertainty about the future rates of return. By their investment behaviour, insurance companies may augment the savings currently flowing in from their policyholders with the proceeds from sales of assets, particularly Government securities, out of their existing portfolios. If these securities are bought by the public with idle money balances or by the monetary authorities, credit is put at the disposal of borrowers which is greater than the funds which savers are currently putting at their disposal.

In addition to the quantitative aspect of their investment policy, the qualitative aspect is also important. This can be seen from the fact that the destination of the savings administered by the insurance companies may have a significant influence on the pattern of fixed capital formation and hence on industrial expansion. It is therefore necessary to examine the effect of the growth of savings through the insurance companies on the supply of funds for industrial development, and the availability of funds to both the public and the private sectors. The distribution of their assets between the obligations of the public and private sectors also has implications for the conduct of monetary and debt policy. In times of increased credit for instance, the effectiveness of the authorities efforts to decrease credit to the private sector can be greatly enhanced if

they can attract a higher proportion of the contractual savings administered by the insurance companies into official hands. Consequently, it is also necessary to study their role in both government finance and public debt management. Thus in assessing the role of insurance companies in the developmental process, it is to be expected that this should be reflected in the trend in their portfolio holdings.

1.4 Objectives of the Study

Among the non-bank financial intermediaries in Kenya, insurance companies are the most important both in quantitative terms (See Section 1.1) and quite apart from the fact that they have had an uninterrupted growth since the end of the war. It is my intention to study the portfolio holdings of these insurance companies, both life and non-life, during the period 1950 to 1974.

In this respect we shall be concerned with:

1. The extent to which changes in the portfolios of the insurance companies have reflected changing demands of the economy.
2. What influences investment policies of insurance companies in Kenya.
3. The role of insurance companies with regard to government finance, the development of the capital market, the public and private sectors.
4. Whether insurance companies have played a role in the developmental process.

1.5 Statement of Hypotheses and Methodology

Hypotheses

In the light of the foregoing, this study is geared to investigating the following hypotheses:

1. That insurance fund managers must be seen as conservative investors who adopt a prudent image and pursue cautious portfolio policies because of their traditional concern for solvency. This conservative investment behaviour is partially due to the fact that insurance business in Kenya is widely dominated by foreign companies whose policy decisions tend to be dictated from their parent companies.
2. That despite the relatively large growth in their accumulated funds, insurance companies have played very little role in the direct allocation of investible funds for development in response to the Kenyan situation. Consequently, apart from investing primarily in short-term assets, they have had only a minimal impact on developing the capital market which is already underdeveloped due to the narrowness of the market for most securities.
3. That unlike their counterparts in the U.S.A. and especially in the U.K., where they have had an indisputable power through their influence on the economy as to even necessitate the indirect use of monetary policy to regulate their activities from time to time, this has not been the case in Kenya

due to their reluctance to influence to any appreciable extent the development process in spite of their relatively long existence in the Kenyan economy.

4. That of late however certain developments suggest that this situation could be changed to make insurance companies increase their role without necessarily resorting to direct control of their operations.

Methodology

In a study of this nature, information required to support the above hypotheses depends on a lot of statistical data. In this respect this investigation relies heavily on available published data between 1950 and 1974. The major source of the data therefore is the East African Insurance Statistics published by the East African Statistical Department up to 1967; for the years 1968 to 1970 by the Central Bank of Kenya and from 1971 onwards by the Central Bureau of Statistics. Other sources of data are the annual published reports of insurance companies obtained from the Registrar of Companies, the annual Statistical Abstracts and Economic Surveys.

Again assembling these data without any interviews of the portfolio managers involved will be quite meaningless. Thus our investigation is supplemented by information collected through personal visits and chats with top management of a number of insurance companies including the State Reinsurance

Corporation and personnel of the Registrar of Insurance Companies Department.

As to the validity of the hypotheses, our investigation will be based on analysis and interpretation of these data as well as drawing comparisons between them and other countries as becomes necessary.

CHAPTER TWO

LIFE ASSURANCE

The objective of this chapter is to isolate life assurance from non-life business and analyse its role in the Kenyan context since independence. In doing so we shall attempt to answer some of the issues raised in the last chapter and thereby investigate to what extent some of our hypotheses could be verified or negated. Section 2.1 is a brief discussion on the nature of life assurance in general while section 2.2 is concerned with the principles and practices that guide investments of life assurance companies. In section 2.3, an attempt is made to evaluate the performance of life business in the Kenyan economy during the post-independence period.

2.1 Introduction

The primary business of life companies is the sale of assurance and annuity protection which enables them to accumulate funds. The need to accumulate life funds is greatly reinforced by the fact that modern life assurance companies "not only protect their policyholders against the danger of dying too soon but also against the danger of living so long that later years of their lives are marred by poverty". [1] Consequently, life

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1. See George Clayton and W. T. Osborn,, "Insurance Company Investment, Principles and Policy". George Allen & Unwin Ltd., London, 1965. pp. 48, 49.

assurance companies receive funds from policyholders seeking protection against financial losses caused by death and poverty in later years of old age. These funds are combined with the aggregate investment of stockholders and are invested in a portfolio of securities that will ensure adequate liquidity to pay policy claims for those policyholders who die or attain policy maturity. Earnings on the invested funds cover a portion of the death claims, since the amount of premium charged on most types of life assurance policy assumes a certain rate of return on the investment of the policyholders' premium payments. This rate of return is contractual, which means that the level of premiums is based upon an assumed percentage rate. If actual earnings exceed this contractual rate, the difference belongs to the owners of the assurance company. but if actual earnings are less than the contractual rate, the shareholders must make up the difference through less earnings for themselves. That portion of the earnings on the assurance company's portfolio that is not allocated for eventual payment of death claims is available to pay the operating expenses of the company and, if anything remains, as earnings attributable to the stockholders of the company.

Underwriting is the process by which an insurance company determines whether and on what basis it will accept an application to insure a particular type of risk. Life assurance is sold to persons wishing to provide financial protection to some beneficiary, usually a family but on occasion a business or

other parties who would otherwise experience a financial loss in the event that the person died prematurely. Because all persons die eventually, the basic business of the life assurance company is underwriting the risk associated with premature death.

The first step in the underwriting process involves determining expected length of life from mortality tables, which have been compiled over many years and which give the ratio of deaths to those living at each age. The second step is to ensure that an adequately large number of policies is sold so that the actual death experience among the many policyholders of each age group approximates the assumptions on which the mortality tables are based. The third step in the underwriting process involves determining what premiums the insured must pay to the assurance company so that total premium receipts in each year, plus possibly a portion of earnings upon the portfolio, are adequate to pay the death benefit claims expected in that year. The fourth step is one wherein the company determines the "load", or amount of operating expenses that must be added to the premium to pay the ongoing costs of the assurance business itself and to provide any underwriting (as distinct from investment) profit.

Life assurance companies sell a wide variety of policies, all of which are combinations of three basic types: term assurance, straight life assurance, and annuities. The simplest type of life assurance is term policy, in which the

the policy runs for a stated period, perhaps five years to ten years, after which it expires. Payment is made to the beneficiary only if the insured dies within the term. An individual straight life, also called ordinary life or whole life, policy provides assurance coverage for a person's entire life unless the policy is terminated by lapse (failure to pay the premium) or surrender for its cash value. Annuities are assurance contracts that guarantee a regular current income for life or for a specified period of years. An annuity for life is, in some respects, the reverse of a straight life policy.

The basic nature of a term policy can be explained with reference to a one-year policy issued to a 23 - year - old person. Let us say, according to one of the tables used by life companies during the period 1950 - 1954 there were 1.89 deaths per thousand persons 23 years old. If the company wrote 1000/- policies on 100,000 persons of 23 years old on the assumption that their mortality experience would duplicate that of the table, the company would anticipate that 189 of these persons would die in the ensuing year. Looking only at assurance the company would have to collect 189,000/- from its 100,000 policyholders in order to have funds to pay 1,000/- for each of the 189 expected deaths. Thus the "pure" premium would be K.Sh.1.89 per insured person.

Most individuals want assurance coverage over a major portion if not the entirety of their life. Term assurance, described earlier, expires at the end of the term and a new policy must be taken out if continued coverage is wanted.

One potential difficulty in obtaining a new term policy to replace an expired term policy is that assurance companies usually require medical examinations for those whom they assure so as to protect themselves against adverse selection by applicants who know they will soon die.[2] As a person ages, he might become unable to pass a physical examination. This difficulty can be overcome by taking out renewable term assurance, in which the policy can be renewed or extended without further medical examination. This is possible because if the renewable provision was stated in the initial policy, there can be no adverse selection several years later at the date of potential renewal.

Term assurance presents another difficulty for the insured, for as he grows older his premium will rise. Continuing with our earlier example of a one-year term policy, rather than the more common five - and ten-year policies, the annual "pure" premium would rise with each decade of age as follows:

Age	'Pure' Premium for one-year term policy of 1000/-
23	KSh.1.89
33	2.32
43	4.53
53	10.89
63	26.57
73	63.26
83	139.38
93	289.30
99	1000.00

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2. See Chapter 1 Section 1.1

As the insured grows old, he would find it increasingly difficult to pay the increasing premium costs. To avoid rising premiums on sequential term policies, one can take out straight life assurance. Under such a policy, a level or a constant premium is paid each year until death, at which time the benefits are paid to the beneficiary. The level premium will be higher than the term premium in early years, but lower than the term premium in later years.

The use of level premium plans makes life companies become investment companies as well. The importance of the level premium plan is that a portion of the premium goes to pay the equivalent of the term premium, while the remainder is invested in a "savings account" for the policy-holder. This savings account, technically called the policyholder's reserve, earns interest at a contractual rate established at the time the policy is written. As the policyholder's reserve builds up over the years through additional premiums plus earnings on past accumulations, it is necessary to "purchase" smaller and smaller amounts of term assurance. At the end of, say, 30 years, the pure premium per 1,000/- of assurance would have risen to 10.89/-. If by this time, however, the policyholder's reserve had increased to, say, 600/-, it would be necessary to purchase only 400/- of pure term assurance at a premium cost of 40 percent of 10.80/- or 4.35/-. By the end of the policy period, the "savings account" would have grown to 1,000/-, and the death benefit payment would amount to giving to the beneficiary the 1,000/- balance in the insured's "savings account".

The level premium type of assurance policy provides funds for the portfolio of the life company. Even a term policy written for five or ten years has itself a level premium over this interval and thus has, to a modest degree, a policyholder's reserve during some of this interval. In any event, the assurance company is receiving funds that it must invest and on which it is calculating an imputed interest rate to add to the reserve of the policyholder. If the life company can earn more on the funds than it has contracted to add to the policyholder's reserve, the difference, as we have already pointed out, belongs to the stockholders of the company. This is offset, however, by the fact that if the funds should earn less than the contractual rate, earnings on the stockholders' equity cushion would have to make up the difference. Generally, contractual rates are set below what the company thinks it will be able to earn.

From the foregoing, we can see that accumulated funds play a vital role in life assurance and basically, the rise of the fund is determined by the difference between two flows, the inflow of premium income and interest earnings minus tax and the outflow of claims and expenses. The volume and time trend of claims depends upon the rate of mortality experienced by the insured. In practice this is calculated by actuaries who use mortality-tables which take into account such factors as, age, sex, and class of life, of which the rate of mortality is a function. The actuarial profession is a highly technical job and at the moment life companies for instance, depend on outside consultants as there are only two qualified actuaries in Kenya who are also expatriates.

Through their operations, life assurance companies come to have large funds under their control. The necessity for the large accumulated funds can be justified on two grounds. First, since it is convenient to sell life assurance in the form of long-term contracts for the payment of equal annual premiums, technical considerations require the accumulation of funds in the hands of the assurance companies for the duration of these contracts. Secondly, in contrast with companies providing other types of insurance, they act as agents and intermediaries for the collection of the public's savings and become liable to repay the capital sums entrusted to them plus interest at some fixed date in the future. The funds, which thus accrue to them from the various types of policy premiums, are earmarked to cover future liabilities which can only be met if they are kept intact and allowed to increase at the compound rate of interest assumed at the time of the initial contract. Despite these reasons and that it is still possible for an assurance company with an apprently large fund available to be technically insolvent, life assurance companies are often criticized for being conservative in theirinvestment behaviour because it is felt their cash flow position is so stable and predictable that a natural built-in liquidity is provided. [3]

2.2 Principles of Portfolio Choice of Life Assurance companies

Clayton and Osborn have pointed out that until recently, there had been little discussion among actuaries on the appropriate investment

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3. Clayton and Osborn, op. cit. pp. 53 - 67.
Also see National Christian Council of Kenya, "Who Controls Industry in Kenya? Report of a Working Party", East Africa Publishing House, 1968, Chapter 15.

policies to be pursued by managers of life and non-life insurance funds. [4] Because of the divergence between the objects served by the two types of insurance funds, principles which would be suitable for one would not necessarily be appropriate for the other. [5] Consequently, whereas a skilful investment policy is crucial to the success of a life assurance company (because of the long-term nature of the business), this is an incidental factor for a non-life insurance company.

In formulating a portfolio policy, that is, a set of principles governing specific decisons to acquire or dispose of portfolio assets, life assurance companies are faced with a choice between portfolio return and portfolio risk.[6] The risk of a life assurance company is rather unique in that the company enters into a contract which promises an interest return from the outset although the receipt of the premiums, and hence the investment, will be delayed until some future date. Portfolio selection under conditions of uncertainty assume that investors consider each category of asset by the characteristics of the probability distributions of the returns attached to it. [7] Using the techniques of portfolio analysis, it is possible to derive the set of what Markowitz calls "efficient" portfolios,

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4. Clayton and Osborn, op. cit.
5. For the dissimilarities between non-life and life insurance see Chapter 3.
6. See Dr. L. D. Jones, "Investment Policies of Life Insurance Companies", Division of Research, Graduate School of Business Administration, Harvard University, Boston, 1968, Chapters 1 and 2.
7. The most influential work on this subject since World War II has been that of Markowitz. See in particular, Markowitz, "Portfolio Selection: Efficient Diversification of Investments", John Wiley & Sons, Inc., New York, 1959.

that is, portfolios which satisfy the requirement that no combination of assets can produce a higher expected return without also incurring greater variability of return. [8]

To illustrate measurement of risk, take r to represent expected value or expected outcome having a wide range of values each with its own probability and defined as $\bar{r} = \sum y_s r_s$ where y_s is the probability that r will take the value r_s. Following this definition, and using as a measure of risk or variability of the return, the variance is $\sum y_s (r_s - \bar{r})^2$, which is the average of the squares of the deviations of the values of the return from its expected value (expected value then is the value of the outcome multiplied by its probability). Thus given an investment fund and assuming that investors desire high expected return and low variability (or risk) of return, they will select a portfolio from among the set of efficient combinations. In so doing, diversification becomes possible as a desirable objective in itself.

Quite apart from practical difficulties in using Markowitz's model, Dr. Jones has also pointed out other obstacles that the theory entails for an empirical investigation into investment behaviour.[9] "The model", for instance, "demands that the investigator be able to specify the statistical moments upon which the investor's utility depends and the form of the functional relationships from which investor estimates of expected value, variance, are determined. But even at this, the model may fall well short of reflecting all the relevant

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8. Markowitz, op. cit., Part III.

9. For instance, computational problems involved in variances and covariances especially when the number of securities is large.

dimensions of the portfolio decision problem. It is not at all clear that variance is an adequate measure of default risk. Higher moments, especially the third moment, are no doubt of significance to many investors. Other characteristics of financial assets, for example, marketability and maturity, are ignored although these attributes are clearly related to portfolio risk. [10]

Despite all these shortcomings, we may note that uncertainty of future events increases the number of relevant attributes to any security and in selecting his portfolio the investor has to choose securities which provide him with the optimum combination of attributes. Thus his demand function schedule for a particular type of security cannot be estimated as the function of its interest-yield alone but other attributes too must be taken into account. Some of the specific attributes that have attracted the attention of writers in the field of insurance are: (1) capital-value risk, or the probability that the market value of a security will fluctuate through time, (2) yield, (3) default risk, (4) marketability or shiftability, that is, the possibility that a security can be easily realized without much danger of loss, and (5) income risk, arising from the fact that interest income cannot be predicted with certainty beyond the maturity and call dates of a security.

How far the above risk attributes influence investment decisions of life assurance companies has been extensively discussed

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10. Dr. L. Jones, op. cit., Chapter 3.

by Clayton and Osborn [11] as well as by Dr. L. Jones. [12] They have shown for instance, that the capital-value risk is of secondary importance because in practice life assurance companies tend to have a stable and predictable built-in liquidity position.[13] For example, the premium inflow of both the U.S.A. and British assurance companies, on average, has been more than twice the outflow of claims and for life companies in Kenya the ratio has been 1.7 (see Table 2 - 2). Furthermore, the need for capital-certainty and marketability are closely connected with the liquidity position of life companies and hence as regards their liquidity preference, the precautionary and speculative motives hardly exist at all. Consequently, their portfolio liquidity can be easily satisfied by placing a nominal amount of their funds in short-term government securities.

A major concern of investment policy is that life companies must earn at least the rate of return assumed in the calculation of the contracts. It is possible that the realized rate of return on invested funds could fall short of the assumed rate. Thus life assurance companies are exposed to an income risk arising from the uncertainty about future movements in the level of interest rates. However, minimization of income-risk, like capital-value risk, does not constitute an important objective of investment policy because of the part played by a bonus loading element in with-profit premiums, which provides a reserve that can bear the brunt of any initial

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11. Clayton and Osborn, op. cit.
12. Dr. Jones, op. cit.
13. Ibid.

failure to earn the rate of return assumed when the without-profit policies were written. Income risk has played little role among Kenya life assurance companies partly because the structure and level of interest rates which prevailed during the regime of the East African Currency Board has been generally maintained although some attention is given to it when investing their funds worldwide rather than in Kenya alone.[14]

The principle of spreading investments is required to minimize the risk of default. Here again, in practice, there does not appear to be a great deal of evidence to support the view that portfolio diversification is deliberately sought as an investment objective. For most life assurance companies the size of the accruing funds, combined with the desire always to keep fully invested, ensures that the desired portfolio diversification is attainable without conscious effort. Invterviews with the investment managers of ten life assurance companies in Kenya have confirmed the impression that few of them if any, consciously make diversification a major objective except in the field of equity investment.[15]

Given that minimization of the four risk attributes are not important objectives of investment policy, it follows that life assurance companies can be regarded as adopting a

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14. See Central Bank of Kenya, "Money and Banking in Kenya", 1973, p. 20.

15. Investigations of Clayton and Osborn also confirm the same attitude among British Life Companies.

particular investment pattern by following the simple objective of maximizing expected yields. Here too we must caution that in practice, there is no conscious effort on the part of life assurance companies to pursue this maximization objective. For one thing, life offices scarcely employ qualified personnel such as investment or financial analysts and economists to manage their portfolios. In most cases, even such a giant institution like the Prudential Assurance Company in the U.K. has started employing such expertise only recently, although the investment department still remains small.[16] Maximization of expected yields also operates under certain constraints which are not of much concern to life assurance companies in Kenya. The first constraint is exposition to currency risks when companies invest worldwide and the incidence of taxation. The principles whereby the liability of life and annuity funds to tax are determined are extremely complex as in the U.K. which is not the case in Kenya where life companies are taxed on their profits just like other non-insurance companies.

To sum up, the needs of life assurance companies in relation to their liabilities are such that they respond in the following manner. They follow a policy of keeping fully invested at all times and interviews with investment managers again confirm that at all times their assets are distributed in such a way that 50 percent are held in fixed interest-bearing stocks and the remaining 50 percent in other assets. They are income-conscious

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16. See for instance, Clayton and Osborn's criticism on the reluctance by life companies to employ investment expertise and their strong urge for the creation of such departments. See Clayton and Osborn, op. cit. pp. 235, 236.

investors who strive to maximize their earnings by selecting their assets from a range of eligible investments, eligibility being determined by limits set on the amount of risk acceptable on any given asset. Again, subject to the constraints imposed upon them by their liability to taxation and currency risks, the objective of expected yield maximization is modified in practice by the desire for some portfolio diversification within their equity holdings. In the next section we shall examine the actual investment policy of assurance companies between 1963 and 1974.

2.3 Performance of Life Assurance Companies

In Chapter One we noted that by independence, the number of life assurance companies had decreased by half mainly because of the nationalization of insurance business in India. By 1974 however, life companies had grown to 19 having reached a peak of 20 in 1972. Quite a number of companies writing both life and non-life business have since been withdrawing from underwritting life policies. One reason for this development is that until lately, foreign life assurance companies were using different mortality-tables in determining premiums for their African and non-African clients. When these companies were therefore required to apply the same mortality tables, some have found it necessary to stop writing new policies arguing it was unprofitable because of the higher risk involved in the African business. Out of the 19 life companies operating in 1974, only 5 were incorporated

in Kenya and their total assets and liabilities stood at K£13.4 million out of total assets of K£45.7 million of all life assurance companies.

The growth in the number of life companies was also reflected in the growth in the number of policies, and amount of insurance in force (see Table 2-1 below). Total number of policies increased by 67 thousand or 95.7% during the period 1964/1974 and the amount of insurance in force also rose by K£75.6 million or 80.9% to K£169.2 million.

TABLE 2-1

LIFE POLICIES IN FORCE AND ASSETS OF KENYA LIFE ASSURANCE COMPANIES, 1964 - 1974

Year	Number of Policies	Amount of Insurance in Force (K£'000)	Total Assets (K£'000)
1964	70,806	93,419	N.A.
1965	74,388	90,788	N.A
1966	79,367	92,873	N.A.
1967	83,909	99,583	N.A
1968	118,983	100,446	30,520
1969	145,617	113,468	31,460
1970	109,994	127,111	33,734
1971	127,569	138,669	38,900
1972	121,042	141,087	39,657
1973	147,167	148,405	42,208
1974	137,032	169,198	45,713

Source: Derived from the Insurance Statistics and the Statistical Abstracts

Although cash demands increased steadily from K£1.7 million to K£8.2 million between 1963 and 1974, net premium income remained positive throughout the period thereby ensuring a stable liquidity position (See Table 2-2).

TABLE 2-2

NET PREMIUM INCOME OF LIFE ASSURANCE COMPANIES, 1963 - 1974

Year	Income (K£'000)	Outgoings (K£'000)	Net Income Available for New Investment (K£'000)	Ratio of Cash Inflow to Outflow	Management Expenses as % of Premium Income
1963	3,413	1669	1644	2.0	18.3
1964	3,705	3039	666	1.2	20.2
1965	3,623	2563	1060	1.9	21.7
1966	3,674	2574	1100	1.9	24.7
1967	4,425	2690	1735	1.6	22.7
1968	7,411	4089	3322	1.8	29.7
1969	12,203	4931	7272	2.5	19.7
1970	7,872	4726	3146	1.7	28.3
1971	12,399	6393	6006	1.9	21.2
1972	10,301	6258	4043	1.6	28.8
1973	10,728	7546	3182	1.4	34.1
1974	11,130	8164	2966	1.4	38.6
			Average	1.7	

Source: Derived from the Insurance Statistics and the Statistical Abstracts

Table 2-2 also indicates that on average premium inflow has been more than one and half times the outflow of claims and other expenses. It should also be noticed that but for management expenses which increased by 589% between 1963 and 1974 this liquidity ratio would be even more impressive.

One reason why management expenses tend to be high for life companies is that the number of new policies issued is large and high initial commissions are paid on new policies. Clayton and Osborn have shown that at that level even if no new policies were sold, the life fund would continue to grow for at least ten years and would not return to the original level for over twenty years.[17] And it is partly for this reason that it is said that the precautionary motive for liquidity hardly exists for assurance companies (see Section 2.2).

Table 2-3 indicates the ratios of premiums to claims in life assurance as compared with non-life business. The average over the period gives some idea of the degree of risk attached to both classes of insurance. The higher the ratio, the smaller the degree of risk. On this basis, the risk to insurers is lower in life assurance than in non-life and that this should be so is understandable in that, contingency in life assurance is remote in the sense that it is postponed for a considerable period. Moreover, the unit of potential loss is small and the degree of catastrophe potentially negligible.

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17. See Clayton and Osborn, op. cit. Chapter 4.

TABLE 2-3

RATIO OF GROSS PREMIUMS TO GROSS CLAIMS, 1963 - 1974

Year	Life Assurance	Non-Life Insurance
1963	4.2	2.0
1964	3.6	2.1
1965	3.9	1.9
1966	3.7	2.5
1967	4.4	2.0
1968	6.0	1.3
1969	8.8	1.2
1970	6.4	2.1
1971	6.2	2.1
1972	6.3	2.1
1973	4.5	2.2
1974	4.6	2.8
Average	5.4	2.0

Source: Derived from the Insurance Statistics and the Statistical Abstracts

During the period 1950 to 1963, the average ratio for life assurance was 3.8 which compares favourably with the average of 5.4 in the 1963/1974 period and indicates that life business was in a stronger liquidity position during the 1963-1974 period. In the light of this, it would have been expected that this would be reflected in the distribution of their portfolio assets through a more flexible portfolio policy. On the contrary, the structure of assets of life companies had not been any different from what it was at the time of independence as Table 2-4 shows.[18]

18. Refer to Table 1-5, Chapter 1.

TABLE 2-4

STRUCTURE OF ASSETS OF LIFE ASSURANCE COMPANIES, 1968-1974

	1968	1969	1970	1971	1972	1973	1974
Total Assets (K£'000)	30,520	31,460	33,734	38,900	39,657	42,208	45,713
(% of Total Assets)							
Cash in Hand	0.0	0.0	0.0	0.0	0.2	0.1	0.5
Balances with Banks, Institutions and Agents	0.6	10.9	7.2	13.1	11.9	12.2	14.8
Investments (Domestic & External) *	43.3	36.5	39.2	33.9	33.8	33.5	30.5
Loans and Mortgages	24.4	26.2	24.7	28.3	26.6	23.5	26.3
Fixed Assets (Including Real Estate/Property)	11.3	14.2	19.2	17.6	16.9	15.2	17.3
Other Assets (Including Outstanding Premiums)	20.4	12.2	9.7	7.2	10.6	13.2	10.6
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Derived from the Statistical Abstracts as revised by the Central Bureau of Statistics at the time of writing.

* Includes: Local and Government Securities and Treasury Bills

A more detailed analysis (see Table 2-5) shows that short-term assets (government and local government securities as well as treasury bills) continued to feature prominently in the investment portfolio of life assurance companies. This was closely followed by loans to the private sector mainly in the form of mortgages rather than direct loans. Investment in fixed (company premises and real estate) also remained the third major source of investment with an average proportion of 15.9% of total assets during the period. Financing the public

sector through direct credit was virtually ignored as can be seen in the table. The figures for "all other" domestic investments represent stocks, shares and debentures (both quoted and unquoted, preference and ordinary).

TABLE 2-5

ANALYSIS OF LIFE ASSURANCE COMPANIES' ASSETS, 1968 - 1974

(% of Total Assets)	1968	1969	1970	1971	1972	1973	1974
Cash, Balances with Banks, Institutions and Agents	0.6	10.9	7.2	13.1	12.1	12.3	15.3
Domestic Investments - Securities/T. Bills*	25.1	25.2	23.4	21.4	21.8	21.7	20.6
All Other	7.5	9.2	12.7	8.2	8.9	8.4	9.3
External Investments	10.7	2.2	3.1	4.2	3.1	3.4	0.6
Loans and Advances -							
Policyholders	8.7	9.1	9.0	9.1	7.5	6.8	6.9
Public Sector	0.9	0.9	0.8	1.1	0.6	0.8	0.2
Private Sector	14.8	16.1	14.9	18.1	18.5	18.3	19.2
Fixed Assets	11.3	14.2	19.2	17.6	16.9	15.2	17.3
Other Assets	20.4	12.2	9.7	7.2	10.6	13.2	10.6
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

* Central and Local Government Securities.

Source: Derived from the Statistical Abstracts

Although an actual breakdown of this figure is not available to determine for instance, the extent of the companies' participation in the Nairobi Stock Exchange, this would be taken as a rough guide. One drawback to this study was the difficulty in obtaining information especially relating to shareholdings of insurance companies. This is made more difficult by the fact that the foreign insurance companies submit to the Registrar of Insurance Companies only consolidated published accounts of their head offices and nothing on their separate

operations in Kenya. Even personal visits to these companies could not help. However, it is interesting to note that at the time of independence shares, stocks and debentures constituted 9.3 percent of the portfolio holdings of insurance companies (see Table 1-5) and by 1974, there had not been any significant changes in this ratio. A comparison with the U.K. for example, shows that by 1960, debentures, ordinary stocks and shares constituted 34.9 percent of total investment portfolio of insurance companies.[19] This investment behaviour of assurance companies in Kenya with regard to their reluctance to participate in the local stock exchange can also be said to be responsible for the slow development of the capital market.[20]

That an undesirably large part of life assurance funds is channelled into short-term assets rather than being invested in development projects is also indicated in the trend in their holdings of cash and deposits with financial institutions. These holdings which were only 0.6 percent of total assets in 1968 increased rapidly to 15.3 percent or K£7.0 million by 1974. A breakdown of this figure shows that the bulk was in deposits with banks and financial institutions with only K£0.3 million representing cash and balances with agents (See Table 2-4). Further evidence of this unwillingness to provide funds direct to industry and development is apparent from analysis of their direct loans and advances to the various sectors

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19. See Clayton and Osborn, op. cit. p. 121

20. Compare with the U.K. or U.S.A. where their influence as institutional investors in the Capital Market is so strong that any small action on their part tends to have tremendous impact on the fluctuations in the market.

of the economy in Table 2-6 below:

TABLE 2-6

ANALYSIS OF LOANS AND ADVANCES BY LIFE ASSURANCE COMPANIES, 1968 - 1974 *

	1968	1969	1970	1971	1972	1973	1974
Total Assets (K£'000)	30,520	31,460	33,734	38,900	39,657	42,208	45,713
(% of Total Assets)							
Government	0.9	0.1	0.8	1.1	0.5	0.8	0.1
Enterprises:							
Agriculture	0.4	0.0	0.0	0.0	0.0	0.0	0.0
Mining and Quarrying	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Manufacturing	0.1	0.1	0.1	0.0	0.0	0.3	0.6
Building and Construction	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Real Estate	2.3	2.6	2.6	0.8	8.4	6.0	0.0
Trade	0.3	0.0	0.3	1.1	0.6	1.1	0.4
Electricity and Water Supply	0.0	0.0	0.0	0.0	0.0	0.0	1.6
Transportation/ Storage/Communications	0.0	0.1	0.6	5.2	0.6	0.5	0.4
Financial Institutions	0.3	0.2	0.4	0.0	0.0	0.0	5.7
Other Business	0.4	1.1	0.6	2.7	2.3	2.1	5.6
Total	3.8	4.1	4.7	9.8	11.9	10.1	14.4
Private Households etc.							
Private Households	6.5	10.4	10.3	8.2	6.0	9.6	6.7
Non-Profit making Organisations	0.7	0.0	0.0	0.0	0.0	0.0	0.0
Total	7.2	10.4	10.3	8.2	6.0	9.6	6.7
Total Private and Public Sectors	11.9	15.4	15.8	18.1	18.4	20.5	21.2

Source: Derived from the Statistical Abstracts

* Note that the figures in this table differ slightly from those in Table 2-4 and 2-5, because Table 2-6 excludes loans and advances to the private sector outside Kenya which the other tables include.

Although our investigation has so far shown that the structure of portfolio holdings of life assurance companies did not reflect changing demands in the economy, we must point out that constraints on the holding of assets may influence their investment behaviour. For example, when we say that life assurance companies did not have any impact on the development of the capital market, we must equally note that this could well be a result of the narrowness of the market for shares and securities. Thus, even though they may be willing to hold certain assets, the lack of marketability may prevent them from doing so. This is in fact the case with the Nairobi Stock Exchange.[21]

Having discussed investment policy of life assurance companies in practice and having assessed their performance in the Kenyan economy during the post-independence era, we now propose to offer brief explanations for why they hold the various categories of assets in their portfolios. First, Kenya Government and Local Government securities and treasury bills have the great advantage for income-cautious investors in that they offer complete security of income up to the date of redemption. Thus, provided that at the time of purchase the yield is greater than that assumed in the calculation of current premium, they are an attractive asset for an assurance company. Again, the fact that they are issued to varying maturity dates, they offer a certain amount of spread over time. With respect to income-certainty, it is true that the

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21. See for instance, D. N. Munga in an unpublished M.B.A. thesis, "The Nairobi Stock Exchange: Its History, Organisation and Role in the Kenyan Economy", University of Nairobi, 1974.

expected yield may fall short of the apparent yield if, before the date of redemption, enforced sales should become necessary during a period of rising interest rates. However, as we have pointed out earlier, financial institutions have enjoyed a stable interest rates since the days of the East African Currency Board. The real disadvantage of these securities is that they offer no protection against inflation. Even in this regard, inflation had not been a serious concern in Kenya until 1973 following a long period of practiacally stable prices.[22] Consequently, during the seven year period of 1968/1974, they made net additions to their holdings in every year except in 1970 (See Table 2-7). Notwithstanding the merits and demerits of Government securities and treasury bills by different companies, investment managers almost without exception consider it prudent to hold a considerable proportion of these assets in their portfolios. Those who consider matching long term assets and liabilities as the best way of reducing risk, will naturally hold them, since they are the only assets with sufficient spread of redemption dates to make such a policy feasible. Even those who do not favour matching much do appreciate the flexibility and manoeuvrability which only the holding of these securities offer; for one thing they can be disposed of at any time without undue loss as the treasury always stands ready to redeem them.

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22. Professor Tony Killick for instance, shows that during the 1960's cost of living rose a little over 2 percent a year until 1971 and 1972 when the annual rate of inflation was 5% and in 1973/74 it rose between 15% and 20% annually. See his article, "Understanding Kenya's Inflation" in The Weekly Review, March 3, 1975, Number 4.

TABLE 2-7

HOLDINGS AND NET CHANGES IN HOLDINGS OF KENYA SECURITIES AND TREASURY BILLS BY LIFE ASSURANCE COMPANIES, 1968 - 1974

Year Ending	Total Holdings (K£'000)	Ratio to Total Assets (%)	Net Change (K£'000)
1968	7,649	25.1	-
1969	7,939	25.2	+ 290
1970	7,881	23.4	- 58
1971	8,344	21.4	+ 500
1972	8,654	21.8	+ 310
1973	9,564	21.7	+ 510
1974	9,412	20.6	+ 248

Source: Derived from the Statistical Abstracts

Non-Government fixed-interest stocks of which industrial debentures and preference stock are the chief examples, are a suitable outlet for the investment of life funds particularly if they are redeemable. Debentures offer considerable security of income and if dated, a large degree of capital safety but suffer from the same disadvantage as government securities in that they offer no protection against inflation. They also suffer from other disadvantages as for instance, they sometimes carry a wide range of optional dates of repayment which reduce their attractiveness for investment managers, particularly those who believe in the principle of matching. Again, they are not actively bought and sold in the market except immediately after they have been issued when they can still be bought free of stamp duty. Consequently, debentures are not a very flexible form of investment.

Preference shares, often referred to as "the friendless orphan of the Stock Exchange", suffer from a variety of disadvantages. They are usually undated but at the same time often carry the option of redemption which may be used to the disadvantage of the lender. This uncertainty, combined with the narrowness of the market, leads to considerable fluctuations in capital values while at the same time income-security is not as great as Government securities and debentures. Finally, like all fixed interest stock, they provide no hedge against inflation.

Equities suffer from the disadvantage that they are subject to serious fluctuations in capital value. On the other hand, they offer protection against the hazards of inflation and a share in the increase in profits and dividends which an expanding economy yields. They do however, involve considerable administrative costs. The real justification of a substantial holding of equities is to secure a high expected yield in the form both of capital appreciaton and dividends. This, nevertheless, cannot be done without attempting to estimate the future prospects of a wide range of companies as a basis for selection. The existing portfolio of ordinary shares must also be constantly reviewed and, if necessary, the composition must be changed in the light of current prices and future prospects. To achieve this end, an expert staff of investment and financial analysts is also required.

The other type of asset which provides a good hedge against inflation, is real property (real estate). Increasing urbanization and the growth of population coupled with other influences combine to raise site values in major cities which result in spectacular capital gains. In one respect, property is superior to equities in that it enjoys greater stability of value. Its main disadvantage is that it is not easily marketable and is particularly sensitive to political influences. Life offices usually confine their investments to blocks of high class property such as offices, flats and shops combined with either offices or flats on good sites. There are considerable administrative costs involved, in that the supervision and administration of land property interests requires the services of a specially skilled department. For this reason, there are wide divergencies of practice among assurance companies in the extent to which they invest in property, and some of them virtually neglect this field.

Finally, mortgages as an important category of assets whose main advantages include a low capital-value risk as compared with all quoted securities and a statisfactory yield. Against this however, they have the disadvantage of considerable income-risk and poor marketability. They also tend to be rather short-term investments for the option of repayment means that the borrower may choose to liquidate his liability at a time when opportunities for satisfactory reinvestment are poor. For example, a company may grant a mortgage for a house purchase at a rate of interest of 7 percent only to find that in ten years, after a general

fall in interest rates, it is repaid at a time when similar mortgages are currently yielding only 4 percent. Mortgages also suffer from the same disadvantage as real property in that the administration of loans and mortgages demands skilled supervision especially in those cases where the security is doubtful. This conflict between advantages and disadvantages produce a great variety of attitude among the companies. Thus all of them tend to have some mortgages in their portfolios because they believe that willingess to help policyholders in this way aids the general business of insurance (this is particularly true of composite offices), but only those companies which have built up specialist departments actively seek to increase their investments in this category.

2.4 Summary and Conclusion

In this chapter we have attempted to accomplish a number of objectives. On discussing the general nature of life assurance business, we took a look at some of the principles and practices that guide actuaries and investment managers in the choice of their portfolios. In this respect, it was pointed out that like all other investors, life assurance companies are confronted with all kinds of risk. The main risk attributes that influence assurance companies were enumerated as capital-value risk, yield, default risk, marketability and income risk. After considering the extent to which each of these risk attributes are important portfolio objectives, we concluded that life assurance companies tend to be more concerned with the objective

of maximizing expected yields. This we noted is so because, they are income-conscious investors who try to maximize their earnings by selecting their assets from an array of eligible investments with eligibility determined by how much risk they are willing to accept on any given asset. We then examined investment policy in practice in the Kenyan context by analysing the distribution of their portfolio holdings during the pre-and post-independence eras. Our objective in this regard was to find out any significant developments during the two periods and to what extent life assurance companies have had any impact on the development process in Kenya. Our investigation showed that there had not been any significant changes in the pattern of their asset holdings in the post-independence period despite the fact that there had been a tremendous growth in their accumulated funds. It was particularly noted that assurance companies continued to invest primarily in short-term assets (Government securities), mortgages, real estate and real property rather than in the directly-productive sectors. Finally, we also tried to give reasons why in general, life assurance companies distribute their assets the way they do, by considering some of the merits and demerits of such assets. One conclusion that becomes apparent from this chapter is that on the whole, investment behaviour of life companies in Kenya did not differ much from the practices of their counterparts elsewhere as the literature on the subject already suggests. Perhaps the dominance of foreign subsidiaries

also partially explains this as found out by the Working Party of the National Christian Council of Kenya that "most of their policy decisions are taken in overseas Head Offices".[23] In the next chapter, we shall follow in a somehow similar way our discussion on the other type of insurance, that is, non-life or general insurance.

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23. See N.C.C.K., "Who Controls Industry in Kenya", op. cit. pp. 181, 238.

CHAPTER THREE

NON-LIFE INSURANCE

Although we isolated and discussed life assurance in the last chapter as well as making a broad classification of insurance business in chapter 1, we deliberately deferred any discussion on similarities and dissimilarities between the two categories of insurance. Section 3.1 of the present chapter therefore will, apart from concerning itself with the nature of non-life insurance, bring out some of the differences and similarities. In section 3.2, we shall discuss the principles of portfolio choice for non-life funds and point out how these differ from portfolio choice of life funds already discussed. Section 3.3 then analyses and evaluates the performance of non-life insurance companies in the Kenyan economy.

3.1 The Nature of Non-Life Insurance

Non-life insurance companies provide financial protection against the loss of one's own property or against liabilities that might arise as the result of injury or loss of property to other people. Some of the risks that non-life insurance companies underwrite were listed in Table 1-6 in chapter 1. In all the various fields of non-life insurance there is the common objective of attempting to eliminate risk by bringing together a sufficiently large number of people who are subject to the same risk and wish

to be protected from it. For statistical purposes the lines of non-life insurance are broadly classified in Kenya as fire; employers' liability (workemens' compensation); motor vehicle; marine, aviation and transit; and miscellaneous accidents.

The nature of non-life insurance business can best be understood by contrasting it with life assurance business from which it differs in several very important respects. The business of non-life insurance has more dissimilarities than similarities, with life assurance. With respect to similarities, about the only one between non-life business and life assurance is that both engage in insurance, an institution which by bringing together a large number of similar risks can predict the total with sufficient certainty so that the uncertain loss hazard for the individual can be reduced to a certain premium cost. While the bulk of life assurance concentrates upon risks of human mortality with the age of individuals as the chief variable, in non-life insurance, risk varies with a variety of factors, such as the type of building material, the kind of occupancy, and the fire protection afforded by the community. Normally, the variables are studied for the industry by a central cooperation rating bureau and each casualty line involves a variety of risk factors.

As regards dissimilarities, the shorter term of non-life insurance contracts stands out. Fire and extended coverage insurance policies for instance are written for one or three years and automobile and most non-life insurance lines are usually written on a one-year basis. After expiration of the

policy, and allowing an appropriate time for filing of claims, no further liability attaches to the company, and the whole premium may be considered to have been earned. What the accountant usually does is to set up the whole premium as a liability at the time of the contract is made and to take part of it into income on a pro rata basis over the brief life of the policy. In doing so, no elaborate formulas are necessary, as in the case of life assurance, to allow for a risk that varies over the contract term, or for compound interest upon a legal reserve.

A second difference is that non-life companies give much more attention to concentration of risk, by writing a diversified portfolio of policies in many different areas so as to better assure themselves that adverse events in one year or in one line of insurance business would not unduly hurt the entire company. Companies also reinsure risks they have underwritten with other companies, passing along to another insurance carrier a portion of both the risk and premium to further spread the risk of loss from unusually large policies or from policies written in a single geographical area.

A third disimilarity is that the amounts of claims against non-life companies vary more widely and adversely than in the life field. Thus claims tend to be influenced by random events such as hurricanes, inflation and partly upon

the cost of replacing the damaged or destroyed asset. Such costs increase with the cost of living and may also vary with such uncertainties as the attitude of a court jury charged with assessing the amount of damages to be paid in a particular liability suit. By comparison, the amount paid out on life assurance policies is fixed by the face value of the policy and the only variable is the time of death.

3.2 Portfolio Choice for Non-Life Funds

In chapter 2, we noted that because of the divergence between the objects served by funds of life assurance and non-life insurance business principles which would be suitable for one would not necessarily be appropriate for the other. And because the accumulation of funds plays a far less role in non-life insurance (due to the nature of the business already referred to above), much less attention has been devoted in insurance literature to the problems of investment by the managers of non-life funds. In discussing the principles of portfolio choice for non-life funds therefore, we shall consider how far portfolio objectives differ from those of life funds. To do this involves an evaluation of the attitudes of non-life insurance companies to each of the various types of investment risks enumerated in the last chapter.

The major source of difference is the contrast between the purposes served by the two types of fund. Unlike life assurance, non-life insurance is essentially of a short-term

nature and the premiums are calculated to do no more than cover the risks underwritten in any given year. If the premium income were constant, it would be unnecessary to accumulate funds, as in the case of life assurance, to meet an increasing risk. But, because claims fluctuate much more erratically from one year to another and in some years, there could be exceptionally heavy claims such as arise from natural disasters like earthquakes, it is necessary in non-life business to amass, in addition to the general reserves for unexpired risks and for outstanding claims, contingency reserves which can be readily mobilized to meet unexpected needs. These contingency reserves are related to the value of the risks underwritten and increased when the value of the retained risk rises.

Since the inflow of annual premiums is needed to meet claims arising during the year, it follows that there is a strong demand for cash arising from the transactions motive. Non-life insurance companies also tend to operate through an extensive network of branches, each of which must have an adequate reserve of cash for the prompt payment of claims. This strong transactions demand for cash is reflected in the much higher proportion of cash and agents' balances in the portfolios of non-life insurance companies than of life assurance companies and this accounts for a major difference in their investment behaviour. Table 3-1 below brings out the differences quite clearly.

TABLE 3-1

HOLDINGS OF CASH AND BALANCES WITH BANKS, AGENTS, AND INSTITUTIONS BY INSURANCE COMPANIES, 1968 - 1974

Year	Life Assurance (K£'000)	% of Total Assets	Non-Life Insurance (K£'000)	% of Total Assets
1968	196	0.6	8,223	64.6
1969	3454	10.9	3399	40.4
1970	2421	7.2	3684	39.8
1971	5097	13.1	3677	38.2
1972	4833	12.1	5554	46.3
1973	5164	12.3	6663	49.1
1974	6960	15.3	8683	53.4
Average	4018	10.2	5697	47.8

Source: Derived from the Statistical Abstracts

But since claims are liable to vary unpredictably, one would expect the precautionary motive for demanding liquidity to be sufficiently potent for the investment managers of non-life funds to place great emphasis on capital certainty and to hold cash and/or extremely liquid assets on this account. Furthermore, since their time horizon is relatively short, one would expect the speculative motive to lead at certain times to an additional demand for cash. However, it would appear from evidence given to the Radcliffe Committee on the Working of the Monetary System that their demand for cash over and above that needed for current transactions is negligible and more, surprisingly, so is their demand for liquid assets with high capital-certainty, such as short-dated government securities (see Table 3-4). The evidence further implied that even exceptional needs for liquidity are largely met from the normal inflow of premiums. On the basis of this Clayton and Osborn conclude

that "in their general business the insurance companies do not meet the risk of an unexpected rise in claims by holding cash in excess of the amount needed for current transactions but by holding a considerable proportion of readily marketable securities".[1] Thus, although the need for liquidity is greater for non-life funds than for life funds, it is satisfied not so much by holding cash in addition to the normal inflow of premiums and short-term assets of capital-certainty value as by investing in highly marketable securities with a spread of maturity dates.

Since in fixing premiums there is no assumption that funds will accrue over time at a definite rate of interest, the investment managers of non-life funds do not concern themselves with income risk and no attention is given to matching and immunization.[2] It remains for us now to consider the importance of yield and default risk.

In discussing these last two risk attributes, we might note here and now that the typical modern non-life insurance company may be described as a mutual club combined with an investment trust. In the light of this, it is an important part of their function to earn as high a yield as possible on the funds subscribed by their shareholders, and hence, much of their investment behaviour may be explained by the desire to maximize yield. Shareholders' capital and free reserves which may be defined as all reserves other than contingency

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1. See George Clayton and W.T. Osborn, "Insurance Company Investment, Principles and Policy", George Allen and Unwin Ltd., London, 1964, p. 84.

2. "Immunization" was first proposed by F.M. Redington, to signify the investment of assets in such a way that the existing business is immune to a general change in the rate of interest.

and technical (policyholders') reserves, are their last line of defence and would only be drawn upon to meet extremely unfavourable underwriting results, so that the companies consider that the primary objective in investing this portion of their funds must be to earn as high an "expected" yield as possible. For, although this aim must be subordinate to that of providing security for the policyholders, an insurance company is apt to be judged by its dividend record and by the margin between investment income and the cost of dividend payments. As Baker puts it,

> "The growth of investment income is an important criterion for investors. They regard the ideal insurance company as one which achieves a rapidly expanding volume of premium income without incurring underwriting losses and, by virtue of an enterprising investment policy, provides a steady growth of investment income and dividend payments. Securities offering the highest returns are usually those with the greatest risks, the longest repayment dates and the least liquidity, so they are not the most attractive for a general (non-life) fund portfolio. It is nevertheless possible at times to select investments which improve the income of the fund without unduly impairing the security of capital". [3]

3. C.J. Baker, "Investment Problems of Non-Life Funds", lecture given to the Insurance Institute of London, on February 2, 1959, p. 4.

Given that a non-life fund needs much larger transactions balances, the investment pattern of the two funds is otherwise quite similar. Thus non-life insurance companies, subject to an over-riding demand for readily marketable assets, also behave as income-conscious investors who strive to maximize their earnings.[4] The major contrast between the investment patterns of life and non-life funds is the emphasis on marketability which is reflected in the non-life funds' higher proportion of medium-dated gilt-edged stock.[5] Furthermore, debentures and preference shares figure less prominently in the non-life funds' portfolios because they lack marketability. Similarly, real property and mortgages, although they have the advantage of high yields, are not considered as suitable for non-life funds because they fail the test of marketability and require specialized knowledge.[6] The greatest similarity between the two funds lies in their demand for ordinary shares to satisfy the objective of maximizing expected yields and hedging against inflation. In practice the manager of a non-life fund may display a stronger bias in favour of high-yielding and more speculative equities for, since his fund is liable to tax both on net capital profits as well as income,[7] it is in a better position than a life fund to choose riskier shares, the losses on the sales of some being offset against the profits of others.

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4. This statement is also however, subject to the same qualification we made in Chapter 2 (2.3) on constraints on holding of assets.
5. As we do not have a breakdown of the time spread of securities held by both classes of insurance, it is difficult to say whether this is also true in the Kenyan situation or not. However as we shall see later, securities and treasury bills are not a major asset in the portfolio of non-life funds as in life funds.
6. See Chapter 2.
7. Not however true in Kenya, as insurance companies are subject to the same company tax as other companies (see Chapter 2).

The aim of maximizing expected yields on a portfolio of adequate marketability is subject to a serious constraint in the form of a variety of regulations imposed by governments. Although some stipulate only that the companies must deposit cash or government securities in proportion to each class of business transacted and allow them considerable freedom in the choice of the remainder of their assets, others specify the categories of permitted securities and even the proportion to be invested in each category. In Ghana, for instance, the law on Insurance Investment Funds in Ghana, requires that all life assurers invest 50 percent of their life funds in Government Securities, while non-life insurers must invest 40 percent of their gross premium income in Ghana, 50 percent of which must be invested in Government Securities.[8] In the next section we shall concern ourselves with how far non-life insurance companies in Kenya have responded in practice to the foregoing general investment principles.

3.3 Analysis of Non-Life Companies

Companies engaged in non-life insurance in Kenya are more than life assurance companies. In 1974, out of 48 companies, 27 were involved in non-life business. This number had in fact dropped slightly from 29 firms in 1972 and 1973. The dominance of foreign companies in the non-life insurance

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8. See, Ghana Economic Review (edited), 1971/72, Editorial and Publishing Services, Accra, p. 265.

business (as we have already noticed with life business) is demonstrated by the fact that out of the total number of non-life companies only 6 were locally incorporated. By 1974, total assets of non-life companies which were K£12.7 million in 1968 had grown to K£16.3 million, an increase of 28.5 percent. It is however interesting to note that although there were only 6 locally incorporated companies they commanded K£8.3 million or 50% of the total assets in 1974 by increasing their assets by K£3.4 million or 69.4% between 1971 and 1974 alone. Although assets of non-life insurance companies have grown over the years, quantitatively, non-life insurance is less important than life assurance business and this becomes clear when we see that while total assets of non-life insurance were K£16.3 million, those of life assurance stood at nearly three times, K£45.7 million, in 1974. Furthermore, if we use their reserve funds as a rough indicator of personal savings, we again find that by 1974, life funds (plus outstanding claims) had reached K£39.9 million as against unexpired risk reserves (plus outstanding claims) of non-life of only K£7.8 million.

There was a tremendous growth in the volume of business by non-life insurance companies during the period 1963/1974. This was reflected in gross premiums earned (written) which increased by K£12.2 million or 349.5 percent to K£15.7 million (see Table 3-2). At the same time management expenses more than doubled (131.8,%) over the same period and thereby reducing income available for new investment to nearly one half (K£7.6 million)

in 1974. Because non-life insurance companies do their business

TABLE 3-2

PREMIUM VOLUME AND UNDERWRITING EXPERIENCE OF NON-LIFE INSURANCE COMPANIES, 1963-1974. (K£'000).

Year	Gross Premiums Earned	Gross Claims Incurred	Management Expenses	Management Expenses as % of Gross Premiums	Net Income Available For New Investment
1963	3,482	1706	1365	39.2	411
1965	3,987	2087	1379	34.6	521
1966	4,835	1912	1383	28.6	1096
1967	4,420	2176	1460	33.0	784
1968	3,946	2985	2570	65.1	(1448)
1969	5,282	4144	2299	43.5	(1009)
1970	7,466	3545	2368	31.7	1745
1971	9,273	4514	2457	26.5	2733
1972	10,296	4900	2709	26.3	3308
1973	11,802	5332	2725	23.1	4302
1974	15,650	5649	3164	20.2	7605

Source: Derived from the Statistical Abstracts.

on annual or short-term contracts, they are able at the end of each year to calculate more precisely than life companies, whether they are making a profit or a loss. It can therefore be seen that during the 11-year period all lines of non-life insurance, except motor vehicle insurance, recorded net positive earnings in every year (see Table 3-3). It is obvious that the losses incurred by motor vehicle insurance accounted for the negative income

available for new investment by non-life insurance as a whole in 1968 and 1969.

TABLE 3-3

NET PREMIUMS EARNED BY NON-LIFE INSURANCE COMPANIES BY LINE OF INSURANCE, 1963 - 1974 (K£'000)

Year	Fire	Workmens' Compensation	Motor Vehicle	Marine Aviation & Transit	Miscellaneous Accident
1963	778	155	472	150	221
1965	722	154	502	250	272
1966	1031	163	804	130	351
1967	1049	175	492	160	368
1968	838	71	(242)	193	201
1969	750	96	(425)	205	512
1970	1459	300	952	554	656
1971	1907	340	640	879	993
1972	1952	379	806	1065	1294
1973	2652	412	1759	162	1485
1974	3156	484	3526	1013	1722

Source: Derived from the Statistical Abstracts

We have already remarked that in distributing their assets, non-life insurance companies tend to hold a large portion in liquid assets such as cash and balances with banks, agents and institutions because of the strong transactions demand for cash (see section 3.2). Table 3-4 shows the structure and trend of assets of non-life companies during the period 1968 to 1974. The table indicates that other major sources of investment for non-life companies were fixed assets (company premises and real estate) and the item,

"all other" (shares, stocks and debentures). With regard to shares, stocks and debentures, we may note that once again, a breakdown of these figures shows that the bulk of this direct participation in financing business came from the 6 locally incorporated non-life companies. Government and Local Government securities and treasury bills also were not an important source of investment for the non-life companies in contrast to the

TABLE 3-4

STRUCTURE OF ASSETS OF NON-LIFE INSURANCE COMPANIES, 1968 - 1974

(% of Total Assets)	1968	1969	1970	1971	1972	1973	1974
Cash, Balances with Banks, Agents and Institutions	64.6	40.4	39.8	38.2	46.3	49.1	53.4
Domestic Investments:							
Security & Treasury Bills	12.7	2.2	3.5	3.2	3.6	4.9	4.2
All Other	0.3	18.8	14.3	19.0	21.0	20.2	17.3
External Investments	2.0	2.1	2.2	1.3	1.0	1.0	0.6
Loans & Advances:							
Public Sector	0.9	1.3	1.0	3.2	1.9	0.7	0.7
Private Sector*	2.3	3.8	2.7	1.5	1.5	2.1	3.2
Fixed Assets	12.8	12.9	11.7	9.0	6.5	10.1	6.2
Other Assets	4.4	18.5	25.4	24.6	18.2	11.9	14.4
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Derived from the Statistical Abstracts

* Includes loans and advances to private sector outside Kenya.

life assurance companies. Between 1968 and 1974 for example, except in 1968 when these purchases were K£1.6 million, they were less than K£1.0 million in all the other years. We saw in the last chapter, the unwillingness of life assurance companies to directlty finance the private and public sectors. Both tables 3-4 and 3-5 show that performance on non-life companies in this respect was not any different.

TABLE 3-5

ANALYSIS OF LOANS AND ADVANCES BY NON-LIFE INSURANCE COMPANIES 1968-1974 *

	1968	1969	1970	1971	1972	1973	1974
Total Assets (K£'000)	12,716	8,410	9,262	9,621	12,001	13,578	16,253
(% of Total Assets)							
Government	0.9	1.3	1.1	3.2	1.9	0.8	0.7
Enterprises:							
Agriculture **	-	0.5	0.4	0.3	-	0.2	0.1
Mining and Quarrying	-	-	-	-	-	-	-
Manufacturing	0.5	-	-	-	0.1	-	-
Building & Construction	-	-	-	-	-	-	0.7
Real Estate	0.2	-	-	-	0.8	1.1	1.0
Trade	-	-	-	-	-	0.1	0.1
Electricity & Water Supply	-	-	-	-	-	-	-
Transportation/Storage/ Communications	-	-	-	-	-	-	-
Financial Institutions	0.6	0.8	0.7	-	-	-	-
Other Business	-	-	-	0.9	0.5	0.4	-
Total	2.1	2.6	2.1	4.5	3.3	2.6	1.9
Private Households etc.:							
Private Households	-	0.8	0.6	0.2	0.1	0.2	1.3
Non-Profit Making Organisations	0.6	0.1	-	-	-	-	-
Total	0.6	0.9	0.6	0.2	0.1	0.2	1.3
Total Private & Public Sectors	2.7	3.4	2.7	4.7	3.4	2.8	3.2

* Excludes loans and advances to private sector outside Kenya

** Includes forestry, fishing and wildlife

Source: Derived from the Statistical Abstracts

3.4 Summary

Our objective in this chapter was not any different from what we had already done in the last chapter. Nevertheless in discussing the nature of non-life insurance business, we pointed out that it was best to do so by contrasting it with life assurance business. Similarly, with respect to the principles and objectives of portfolio choice for non-life funds, we also considered how far they differ from those of life funds by evaluating the attitudes of non-life insurance companies to each of the various types of investment risks referred to in Chapter 2. We noted that non-life insurance companies, subject to an over-riding demand for readily marketable assets, also behave as income-conscious investors who strive to maximize their earnings. In our analysis of their actual portfolio holdings during the period 1968/1974, we found some differences in the structure of assets of non-life and life companies. In the first place, whereas non-life companies held an average of 50 percent of their assets in cash and other near-cash assets, life companies held an average of only 10 percent during the period. Secondly, in contrast to life assurance companies, non-life companies did not give any loans and advances in the form of mortgages and this was also reflected by the fact that no loans and advances were given to policyholders (see Table 3-4). On the other hand, changes in the composition of the portfolios of non-life companies were not much different from those of life offices. With regard to their role in the developmental process and their impact on the economy, we found that non-life companies featured even less significantly than life assurance companies.

CHAPTER FOUR

SUMMARY AND CONCLUSIONS

The basic assumption that lies behind this study is that although in quantitative terms insurance companies are the most important among the non-bank financial intermediaries in this country, little or practically no work has been done to analyse the role they have played so far in shaping economic development despite their relatively long existence. If we are to understand and appreciate the impact of insurance companies on the economy, it is essential to assess and evaluate their relative significance as controllers of large investible funds, to analyse their investment behaviour as well as their performance in the various sectors of the economy. It is precisely this which we have attempted to do in the foregoing pages and the time has now come to put together the various strands and look at the picture as a whole. Having done that, we will be able to make some conclusions and some recommendations for broader policy issues as well as suggest problems for further study.

4.1 Summary

In establishing their importance as collectors of large funds, we have found that between 1964 and 1974 the assets of all insurance companies grew by an average of 13 percent per year and there is no evidence as yet of any slackening in the

pace of expansion. What is more, the volume of life assurance in particular is steadily growing and since the rate of growth is based on a rising level of real income per head as well as on a rising birth rate, the prospect is for further substantial rises in the volume of life assurance being written.

A second feature of their role as savers is that the savings which they administer are contractual and, therefore, relatively stable. Thus of all the various forms of types of personal saving they are least likely to fall if income falls. This means that the investment managers of life companies must frame their policies in the knowledge that week by week funds will continue to flow in to their tills as a result of past sales of policies.

Having assessed their importance among the non-bank financial intermediaries, our next task was to consider the motivations behind their investment behaviour. So far as life funds are concerned we found that investment managers do not pay particular attention to the avoidance of capital-value risk and income-risk but follow the objective of maximizing expected yield. We however qualified this objective by saying that in practice there is no conscious effort by them to pursue it for various reasons. [1] There is little reason to believe that this maximization rule is modified in practice by the conscious pursuit of portfolio diversification to avoid

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1. See Chapter 2 (2.3)

the risk of default, except in their choice of ordinary shares. We also saw that life assurance companies may be described as income-conscious investors who strive to maximize their earnings by choosing from a range of assets, eligibility being determined by limits set on the amount of risk acceptable on any given asset. In practice the desire to attain this objective is subject to constraints imposed by taxation and currency risks. So far as non-life funds are concerned, the picture is similar except that they have a greater transactions-demand for cash and place greater stress on marketability.

In our analysis of insurance companies' investment behaviour we have also observed certain characteristics. First, although in the literature of general economics it is frequently assumed that insurance companies, like individual investors, pay attention to liquidity as well as to safety and yield, we noted that life offices have virtually no need for liquidity as this term is usually understood. The high degree of stability, and the magnitude of their net cash inflow makes the idea of liquidity preference have little meaning for them. Since today's cash flow is largely determined by the rate of policies in the past, the future cash flow may be calculated from the rate of sales up to the present. We have noted for instance that the past rate of growth of Kenyan assurance companies has been such that, on average, premium inflow has been more than one and a half times the

outflow of claims; this natural built-in liquidity is sufficient to withstand emergency demands for cash with little strain. However we could also talk of a need for liquidity of a different sort from that usually meant by the term "liquidity preference". This need for liquidity does not arise from the external demands of policyholders but from internal considerations concerned with the management of their portfolios. Although life companies may remain fully invested in the sense that their holdings of cash and other liquid assets form a negligible proportion of their total assets, they can and do shift some proportion of their funds from one category of investments to another when differentials in yield make this desirable. They would be unable to take advantage of such favourable opportunities unless they held in their portfolios some assets which possessed the attribute of shiftability. It is for this among other reasons, that they find it essential to hold some Government securities in their portfolios.

A second important characteristic which is to some extent the obverse of the first, is that the funds of insurance companies are directed in a regular and uninterrupted flow into various outlets for investment. In their investment behaviour they aim at all times to keep fully invested. Thus although a considerable amount of effort is devoted to the forecasting

of future rates of interest, investments do not appear to be made on the basis of expectations. As O'Leary puts it, "the typical financial officer stresses the cost, in the way of foregone interest, of trying to guess a change in rates and he figures that under most circumstances and on the average he would be better off to invest the money at the going rate than to hold funds liquid in expectation of a rate rise".[2]

A third characteristic is that they are not normally dealers in securities but are true long-term investors who purchase securities to hold for income. To some extent such an attitude is forced upon them because the growth of their funds has increased the degree of imperfection in the capital market. This imperfection and influence in the capital market become clear when we note that in the U.K. for example, a colossal institution like the Prudential Assurance Company made net new investments of £147 million during 1972 (this amounts to some £2.8 million weekly!)[3] In this way the large companies in particular tend to dominate the market to the extent that it is extremely difficult for them to unload their holdings without moving the price against themselves.

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2. J.J. O'Leary, "The Institutional Saving-Investment Process and Current Economic Theory", American Economic Review, Volume. 44, May 1954, pp.460,461.

3. See the 124th Annual Report and Statement of Accounts for the year 1972, Prudential Assurance Company Ltd.

At the end of Chapter 1, we stated that our investigation of the insurance companies in Kenya had among others, the following objectives: to examine the extent to which changes in the portolio holdings of insurance companies have reflected changing demands of the Kenyan economy; the role of insurance companies with regard to government finance, the development of the local capital market, the public and private sectors; whether insurance companies have played a role in the developmental process; and what influences investment policies of insurance companies. We shall now summarise our findings in the light of these objectives except for the last one which we have already dealt with in the earlier part of this section.

As to the first objective, we have shown in the earlier pages of this study that during the pre-and post-independence eras, there was a large accumulation of funds by insurance companies with premium inflows far outpacing cash outflows and thereby leaving large balances for new investment. We also noted in Chapter 1 that at the same time throughout the period covered by our study, the economy recorded a stable growth with practically no constraints in the way of say, inflation. It would therefore have been expected that insurance companies would respond to the changing demands of the economy in the choice and distribution of their portfolio holdings. On the contrary, our investigation has shown that there was no significant departure from what the structure was during the

pre-independence period. This investment behaviour we pointed out was not uncharacteristic of their counterparts elsewhere as insurance fund managers are conservative investors who tend to adopt a prudent image and pursue cautious portfolio policies due to their traditional concern for solvency. Furthermore, we noted that this investment attitude is partially attributable to the fact that insurance business in Kenya is by and large dominated by foreign companies whose policy decisions tend to be dictated from their Head Offices abroad. Thus in spite of the continued large growth in their accumulated funds, insurance companies invested primarily in short-term assets such as local and government securities, bonds and treasury bills.

With respect to their impact on the capital market, although a Stock Exchange has officially been in existence since 1955, the insurance companies have been virtually reluctant to participate in the market for stocks and shares and thereby contributing to low activity and narrowness of the market for securities. This unwillingness on their part to help develop and expand the capital market through their activity in the local Stock Exchange is rather in sharp contrast to the indisputable power and influence which their counterparts have come to wield as institutional investors in this respect in countries like the U.K. and the U.S.A.

Following our discussion on the distribution of their assets, we have seen that the insurance companies have been an important source of Government funds both on long-term basis (through stock purchases) and on short-term basis (through deposits with the Cereals and Sugar Finance Corporation).[4] In this respect they have been active in providing a market from which Government borrows substantially, loanable funds to finance the amount of its expenditure not provided for by tax receipts and other sources of revenue.

In our analysis of direct loans and advances of the insurance companies, we observed that their performance in financing the private and public sectors of the economy has not been encouraging. Whatever funds they provided for private sector finance were mainly channelled into real estate in the form of mortgage loans.

From the foregoing, we can say that if the insurance companies have had any role to play at all in the developmental process of Kenya, the response has been mainly indirect through the financing of the central Government and quasi-Government institutions rather than directly investing in development projects.

4.2 Conclusions

On the basis of what our study has revealed we can make a few conclusions:

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4. The Cereals and Sugar Finance Corporation provides a channel to Government of short-term finance as the agent of the Treasury in respect of financing specified cereals and sugar.

1. That by virtue of the large accumulated funds under their control, the role of fiduciary responsibility for individual savings is likely to become more important with rising incomes and increasing awareness on the part of the public to take up policies.
2. That as the capital market becomes more developed and organised, the insurance companies would begin to assert their hitherto latent influence on it and emerge as the true institutional investors that their counterparts in the developed countries have been.
3. That if the present economic philosophy of stress on market economy prevails, insurance companies are likely to see themselves operating in the same competitive atmosphere without any direct control of their activities. And in this respect the dominance and influence of the foreign companies in the business could only be lessened indirectly and through competition from more locally incorporated companies.
4. That unless insurance companies see themselves in a different perspective and change their conservative investment behaviour, they will continue to have no appreciable direct impact on the economic development of Kenya.

4.3 Recommendations for Broader Policy Issues

That insurance companies as well as the many other financial intermediaries will continue to function in the Kenyan economy cannot be denied. If this is so, then this study will not be complete if we do not make any recommendations that may help to increase the role of insurance companies in the development effort.

We have noted elsewhere in this study that until recently life assurance was confined mainly to non-Africans. Consequently, standards for underwriting African lives have been strict and the choice of policies available to them has been restricted. It was because of this discrimination that the Government entered the field of insurance by setting up the Kenya National Assurance Company in 1964 in which it is now the sole shareholder. The company provides a wide variety of life assurance and group pension facilities specially tailored to suit African requirements. Apart from doing this, we have also noted that of late the foreign assurance companies have been required to apply the same mortality tables to both African and non-Africans. Instead of solving the problem of African mortality, this action has rather resulted in the gradual withdrawal of some foreign companies from underwriting new life policies. We understood from one of our interviews that the idea of compiling an African mortality table had been initiated some time ago among the three East

African partner states and would have been the first of its kind in Africa, but broke down after a series of meetings for various reasons. We think that a mortality table for Africans is a laudable idea and therefore suggest that efforts be made to compile such a table. The working party must not be limited to the three countries only but bring together actuaries and other experts from other African countries under the auspices of the African Development Bank which has started a venture in insurance, the African Insurance Corporation, embodying all O.A.U. countries, or under the auspices of the Economic Commission for Africa.

To spread risks, we have seen that insurance companies reinsure with reinsurance companies elsewhere. As this involves foreign exchange, such transactions have had negative effects on Kenya's Balance of Payments and between 1968 and 1974 for example, foreign transactions of insurance companies recorded a net average outflow of K£730 thousand during the 7-year period with the highest being K£2.7 million in 1970 alone. It was not surprising therefore that in 1971, the State Reinsurance Corporation was set up with the basic objective of helping to "domesticate" Kenya's foreign exchange reserves. We see the establishment of the SRCK as a means of regulating and supervising the insurance business beyond merely reinsuring specified amounts of their premiums with it. It has been suggested before that with

the KNAC in Government control, the Government should have "a foot in the door" of the insurance industry, enabling it to assess from the inside whether their premiums are reasonable, their operations efficient, their dealings just, their profits fair and their investments in Kenya's interests.[5] The SRCK should be empowered to collect returns and data from the insurance companies on the various aspects of their activities. The SRCK should also be used as indirect means of diverting their funds into viable development projects requiring them to deposit a certain percentage of their premium income with it if it is felt that the insurance companies are not responding satisfactorily to the Kenyan situation.

There is a strong need to introduce legislation to have all insurance companies incorporated in Kenya. This is necessary to ensure proper control of the activities of insurance companies especially the foreign ones. We have already pointed out our inability to get more detailed or even simple breakdowns of certain items on the published data because foreign insurance companies do not publish separate accounts of their Kenyan operations. Thus at the moment there is too much secrecy surrounding the insurance companies' activities. For purposes of policy and development planning it is therefore recommended that local incorporation would require them to make their activities more public. It is hoped that when the President declared recently

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5. See N.C.C.K. "Who Controls Industry in Kenya?", Report of a Working Party, East African Publishing House, 1968, p. 184.

that "some substantial amendments to insurance laws will be introduced to conform with the needs and aspirations of our African society", he had in mind also the question of local incorporation. [6] Such an amendment will also bring the laws governing insurance business in line with various U.N.C.T.A.D. resolutions on insurance in developing countries.

To accelerate the Kenyanisation process, it is also recommended that apart from being locally incorporated, insurance companies be required to go public with not less than forty percent of their shares being owned by Kenyans. This will also be in conforming with U.N.C.T.A.D. resolutions which other developing countries are gradually implementing.[7]

We feel that a serious look at and adoption of these recommendations plus the noticeable developments already referred to could make insurance companies increase their role in the economy without necessarily resorting to a direct control of their activities.

4.4 Problems Suggested for Further Study

Although we have noted that little or no work has been done on insurance companies in Kenya, it would equally be naive

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6. See Daily Nation of 12th June 1976.

7. Ghana in 1973 amended the Insurance Act (1965) by N.R.C.D 95 introducing an obligatory local incorporation and selling not less than 40% of shares to Ghanaians (see the Bank of Ghana Annual Report, 1973.)

to pretend that this study exhausts all the possible problem areas of research on the insurance business. What we have attempted to do in the preceding pages is only to serve as an aid to future research by others in the field of insurance. That we have stated some limitations to the available data, further suggests that there is more to be done when such data become available. One area that we have not touched on is examining the nature of the savings which the insurance companies administer and their relative importance as compared with other sources of savings. There is also the question of examining the desirability and feasibility of subjecting them to official control and regulation to protect the public interest.

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