EFFECT OF BANCASSUARANCE ON FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

PRESENTED BY

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OCTOBER 2013
DECLARATION

STUDENT’S DECLARATION

I declare that this project is my original work and has never been submitted for a degree in any other university or college for examination/academic purposes.

Signature: ……………………………………Date:……………………………………

EVANGELINE MWATI REG NO: D61/6379/011

SUPERVISOR’S DECLARATION

This research project has been submitted for examination with my approval as the University Supervisor.

Signature……………………………………….Date…………………………………..

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DEDICATION

This work is specially dedicated to my dear brothers and sisters Nicholas, Alice, Lucy and Alex for believing in me and their relentless support and encouragement in my studies. Your encouragement and support has brought me this far.
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Thanks to the University of Nairobi librarians for availing much needed documents for the study. They were always available to direct me on where to find the different literature materials required for this research.

My heartfelt thanks also go to the management of all the commercial banks and the Central Bank of Kenya who participated in this study.

Thank you to all my friends who contributed to the completion of this academic document both directly and indirectly. You all provided me with logistical and moral support that gave me every reason to work harder and ensure that this study becomes a success.
ABSTRACT

Over the past decades, fundamental changes in the industry of financial intermediation, such as deregulation and advances in technology, had a visible impact on the provision of financial services. Deregulation, in various parts of the world, has made flexible the provision of financial services and promoted competition among financial institutions. In Kenya, this has seen the entry of Mobile telecommunication companies into banking industry thus limiting commercial banks revenues substantially. One of the most prominent transformations undergone by the financial services industry has been the emergence and expansion of bancassurance (or bank-insurance). Despite the importance of this issue, few empirical analyses have directly assessed efficiency issues in the bancassurance business and, as far as the researcher is aware, none of these focused on performance differences among alternative forms of cooperation between the banking and the insurance industries. This is despite the fact that most of the commercial banks in Kenya are adopting bancassurance services without any tangible effect on their financial performance.

The purpose of this study was to establish the effect of bancassurance on financial performance of commercial banking industry in Kenya. This study was a descriptive survey. The target population of this study was the nine commercial banks in Kenya that have taken up bancassurance. Due to the population size of commercial banks in Kenya that have taken up bancassurance, the research took the census approach. The secondary data was collected from the commercial banks audited financial statements and also CBK for the year 2008-2012. Data was analyzed using Statistical Package for Social Sciences (SPSS Version 21.0) program. The data collected was run through various models so as to clearly bring out the effects of bancassurance on bank financial performance.

The study concludes that bancassurance has a weak positive but significant influence on the financial performance of commercial banks in Kenya. The study recommends that the study recommends that the bank managers should promote the adoption of the bancassurance to their customers through advertising to its customers most of whom are not insured. Intense market competition between banks has led to a substantial decrease in the interest margins of the traditional banking products. Banks should take advantage of widespread branch network across the country in the distribution of insurance products.
# TABLE OF CONTENTS

DECLARATION................................................................................................................................. ii
DEDICATION....................................................................................................................................... iii
ACKNOWLEDGEMENTS...................................................................................................................... iv
ABSTRACT.......................................................................................................................................... v
TABLE OF CONTENTS...................................................................................................................... vi
LIST OF TABLES............................................................................................................................. ix
LIST OF ABBREVIATIONS.................................................................................................................. x
CHAPTER ONE ..................................................................................................................................... 1
INTRODUCTION ............................................................................................................................... 1
1.1 Background of the Study............................................................................................................... 1
1.1.1 The Concept of Bancassurance......................................................................................... 1
1.1.2 Financial Performance......................................................................................................... 2
1.1.3 Bancassurance and Financial Performance ..................................................................... 4
1.1.4 Commercial Banks in Kenya........................................................................................... 5
1.2 Statement of the Problem.......................................................................................................... 6
1.3 Objectives of the Study ............................................................................................................. 7
1.3.1 General Objective ............................................................................................................ 7
1.3.2 Specific Objectives .......................................................................................................... 7
1.4 Significance of the Study.......................................................................................................... 8
CHAPTER TWO ................................................................................................................................... 9
LITERATURE REVIEW .................................................................................................................... 9
2.1 Introduction .............................................................................................................................. 9
2.2 Theoretical Review .................................................................................................................. 9
| 2.2.1 Modern Portfolio Theory (MPT) | ................................................................. | 9 |
| 2.2.2 Classic Finance Theory | .......................................................... | 10 |
| 2.3 Empirical Review | ......................................................... | 11 |
| 2.4 Conclusion | ......................................................... | 14 |
| CHAPTER THREE | ...................................................................... | 16 |
| RESEARCH METHODOLOGY | ...................................................................... | 16 |
| 3.1 Introduction | ................................................................... | 16 |
| 3.2 Research Design | ................................................................... | 16 |
| 3.3 Target Population | ........................................................................ | 16 |
| 3.4 Sampling Procedures | ........................................................................ | 17 |
| 3.5 Data Collection | ........................................................................ | 17 |
| 3.6 Data Analysis Methods | ........................................................................ | 17 |
| CHAPTER FOUR | ...................................................................... | 18 |
| DATA ANALYSIS, RESULTS AND DISCUSSION | .................................................................. | 18 |
| 4.1 Introduction | ................................................................... | 18 |
| 4.2 Regression Results | ................................................................... | 18 |
| 4.2.1 Year 2008 Analysis and Interpretations | .................................................. | 18 |
| 4.2.2 Year 2009 Analysis and Interpretations | .................................................. | 21 |
| 4.2.3 Year 2010 Analysis and Interpretations | .................................................. | 22 |
| 4.2.4 Year 2011 Analysis and Interpretations | .................................................. | 25 |
| 4.2.5 Year 2012 Analysis and Interpretations | .................................................. | 24 |
| 4.3 Summary and Interpretation of Findings | .................................................. | 25 |
| CHAPTER FIVE | ...................................................................... | 28 |
| SUMMARY, CONCLUSION AND RECOMMENDATIONS | ................................................................ | 28 |
| 5.1 Summary | ................................................................... | 28 |
5.2 Conclusions .................................................................................................................. 29
5.3 Recommendations for Policy and Practice................................................................. 30
5.4 Limitations of the Study ............................................................................................ 31
5.5 Suggestions for Further Research ............................................................................ 31
REFERENCES ............................................................................................................. 33

Appendix I: Commercial Banks Offering Bancassurance Services .............................. 37
LIST OF TABLES

Table 4.1: ANOVA Statistics for 2008 Data ................................................................. 18
Table 4.2: Coefficients of 2008 Model ........................................................................ 20
Table 4.3: ANOVA Statistics for 2009 Data ................................................................. 21
Table 4.4: Coefficients for 2009 Regression Model .................................................... 21
Table 4.5: ANOVA for 2010 Statistics ........................................................................ 22
Table 4.6: 2010 Model Coefficients .......................................................................... 24
Table 4.7: ANOVA statistics for 2011 Model ............................................................... 25
Table 4.8: Coefficients of model 2011 ....................................................................... 25
Table 4.9: ANOVA Statistics for 2012 ....................................................................... 24
Table 4.10: Coefficients of model 2012 ................................................................... 27
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ATM</td>
<td>Automated Teller Machine</td>
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<tr>
<td>BAs</td>
<td>Bank Assurers</td>
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<td>CBK</td>
<td>Central Bank of Kenya</td>
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<td>CBK</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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<td>ICT</td>
<td>Information and Communications Technology</td>
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<td>KBA</td>
<td>Kenya Bankers Association</td>
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<td>MPT</td>
<td>Modern portfolio theory</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<tr>
<td>ROE</td>
<td>Return on Equity</td>
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<td>SPSS</td>
<td>Statistical Package for Social Sciences</td>
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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

As a result of the globalization and liberalization of the financial services industry, many financial institutions are participating in the business activities of other financial institutions, banks and insurance companies in particular. Often, banks calculated that creating a subsidiary engaging in insurance services, or perhaps both a life and a non-life subsidiary, would create good synergy, as they could market the insurance products via branch unit locations (Voutilainen, 2005). One of the most significant changes in the financial services sector over the past few years has been the appearance and development of bancassurance. Banking institutions and insurance companies have found bancassurance to be an attractive – and often profitable – complement to their existing activities. The successes demonstrated by various bancassurance operations, although not all of them have been successful, have attracted the attention of the financial services sector, and further new operations continue to be set up regularly.

Deregulation that allows for diversification across both financial services as well as geographic areas together provide a potent rationale for the growth of banking and insurance combinations in the years ahead. As a result, mergers between commercial banks and insurance companies have the potential to fundamentally change the financial landscape of a country. However, that potential will become reality only if the bancassurance model is, in fact, a viable one. Unfortunately, there currently exists little direct empirical evidence on the value and risk implications of this form of business combination (Casu and Girardone, 2004).

1.1.1 The Concept of Bancassurance

Many authors have observed that banks and insurance companies as businesses provide services that have more similarities than differences, which favors their joint production. Both types of firms are financial intermediaries that pool savings of individuals and subsequently channel these funds to capital expenditures. Laws of large numbers, economies of scale, liquidity creation, and risk management are common to both institutions (Voutilainen, 2004). It is not surprising that they offer similar products to compete for public savings funds. Also, banks regularly offer loans
and sell insurance to protect against default and property loss. Historically, bancassurance was most developed in France and the Netherlands in the 1980s, due in part to tax-advantaged insurance products made available through banks, in addition to the distribution network and public confidence advantages for banks (Staikouras and Nurullah, 2008).

Banks increasingly have used relationship pricing whereby customers purchasing a number of financial services receive better pricing than single-product customers. Consequently, bancassurance has been growing more rapidly in Europe than banking--securities combinations. One explanation for the success of bancassurance is that bank-insurance combinations are beneficial to both entities in terms of spanning both short- and long-term liability/asset structures in the financial intermediation process and better attracting and retaining retail customers and corporate clients (Voutilainen, 2005).

In the past, as observed by Li, (2006), a credit market hierarchy existed among private debt (inside bank loans), private placements (inside insurance company bonds), and the public debt market (outside debt). Legal barriers affecting the sources of funds among different financial institutions logically led to asset specialization of institutions (e.g., long-term vs. short-term lending) on the supply side of the credit market. For example, owing to the traditional legal separation of banking and insurance underwriting, the majority of bank credit is financed by short-term, floating-rate deposits, whereas life insurance companies obtain funds to invest in bonds from long-term, fixed-rate insurance contracts. Importantly, deregulation eliminated these legal barriers and allowed banks and insurance companies to exploit their joint advantages with respect to both short- and long-term funds in the financial marketplace.

1.1.2 Financial Performance

The organizational performance construct is probably the most widely used dependent variable in organizational research yet it remains vague and loosely defined. The focus of attention in performance has been mainly on financial measures but some scholars have proposed a broader performance construct of ‘business performance’ to incorporate non-financial measures such as market share, customer satisfaction and new products among others. Datta (2006) proposed four possible types of measurement for organizational performance namely: outcomes (turnover, absenteeism, job satisfaction); organizational outcomes (productivity, quality, service); financial
accounting outcomes (return on assets, profitability) and capital market outcomes (stock price, growth, returns). The idea behind this model is that outcomes are hierarchical in that, outcomes at one level impact on those at the next level. In this particular case, participation and commitment in budget process would have the most direct impact on the performance of the individual, which in turn contribute to organizational performance.

According to Bresman and Nobel (2009), the success of an organization is gauged from several indicators both qualitative and quantitative. These include: financial performance, meeting customer needs, building quality products and services, encouraging innovation and creativity and gaining employee commitment. The extent to which an organization succeeds in these areas determines its performance. Performance measures are cost oriented or non cost oriented and can also be internal or external. Casu and Girardone (2004) recognize the difficulty in obtaining objective measures of performance organizations. They also point out that when dealing with organizations in different sectors, standardization is not possible and asking managers to assess their own firm’s performance relative to others in the same industry or sector is an acceptable option. To minimize the effects of random errors, researchers have suggested the use of multiple items and multiple respondents to assess performance.

The financial performance of institutions is usually measured using a combination of financial ratios analysis, benchmarking, measuring performance against budget or a mix of these methodologies. The common assumption, which underpins much of the financial performance research and discussion, is that increasing financial performance will lead to improved functions and activities of the organizations. The subject of financial performance and research into its measurement is well advanced within finance and management fields. It can be argued that there are three principal factors to improve financial performance for financial institutions; the institution size, its asset management, and the operational efficiency (Li, 2006).

Financial performance is a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues. This term is also used as a general measure of a firm's overall financial health over a given period of time, and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Berger, 2001). There are many different ways to measure financial performance, but all measures should be taken in aggregation. Line items such as revenue from operations, operating income or cash flow from
operations can be used, as well as total unit sales. Commercial banks are the major mobilizes and disbursers of financial resources. They have an all pervasive role in the growth of a developing country like India. The role of banks in accelerating the economic development of a country like India has been increasingly recognized.

1.1.3 Bancassurance and Financial Performance

Bancassurance as a way of financial conglomeration has appealed widespread attention in the world of academics and business. It offers consumers a ‘one-stop-shop’ option for a larger range of financial product. This form of a complete financial conglomeration has rapidly grown since the 1980s when interest margins on loans decreased steadily and banks started exploring new sources of revenue. As from the early 1990s, bancassurance has become a major distribution channel in many insurance markets. The sales channel is particularly present in South European markets, but the business the business model is used in other regions as well. Noteworthy is the growth of bancassurance in a broad set of emerging economies (Vander, 2002). The opportunity to tap from different client segments combined with the chance to offer one-stop-shop financial services have globally persuaded both banks and insurance companies to merge their activities.

The distribution of insurance products through a bank’s distribution channel brings diversification advantages by generating non-interest related income. Both insurers and banks are financial intermediaries that pool savings of individuals to channel these funds to the capital markets. The bancassurance model could eventually create cross-selling business synergies for banks that in turn can lead to cost savings through economies of scope. On top of that, financial conglomeration puts institutions in a position to become full service financial firms. To offer a wider range of services is beneficial for bank assurers (BAs) that opt for relationship management and could in the end bring comparative advantages over regular commercial banks and insurers (Kim and Mauborgne, 2005).

Banks are now major distribution channels for insurers and insurance sales have formed a significant source of profits for banks (Staikouras and Nurullah, 2008). The latter partly being because banks can often sell insurance at better prices (i.e., higher premiums) than many other channels, and they have low costs as they use the infrastructure (branches and systems) that they
use for banking. Banking institutions and insurance companies have found bancassurance to be an attractive and profitable complement to their existing business activities (Kirui, 2009).

1.1.4 Commercial Banks in Kenya

There are forty three commercial banks in Kenya as at December 2011(www.centralbank.go.ke). Thirty of the banks, most of which are small to medium sized, are locally owned and thirteen are foreign owned. The banks have come together under the Kenya Bankers Association (KBA), which serves as a lobby for the banks’ interests and addresses issues affecting member institutions (www.pwc.com).

The Central Bank notes that advancement in Information and Communications Technology (ICT) in the banking industry has enhanced efficiency and improved customer service. This is reflected particularly in the increased use of ATM cards resulting from broadening of ATM network, including additional ATM machines and a wider network of merchants that accept payment through credit/debit cards. Several banks have also entered into the Internet Banking and established websites. Internet banking however is still at its infancy and more in terms of utilization is expected in this sector.

The level of competition between banks is therefore very high to attract the retail customers as just their numbers there comes in a big chunk of business either in form of deposit or loans. There has been a shift from waiting for the customers to come to the banks, to now the bank going out of its way to look for the customers. Commercial banks have now adopted strategic issue management to succeed in a world of competition.

Banks are now a major distribution channel for insurers as is evident from Equity, Chase, CFC Stanbic, Diamond Trust, Kenya Commercial Bank, Barclays Bank of Kenya, Commercial Bank of Africa, National Bank of Kenya and Cooperative Bank all of which have adopted this method and insurance sales as a significant source of banks growth. The latter is partly because banks can often sell insurance at better prices than many other channels, and they have low costs as they use the infrastructure that they use for banking (Omondi, 2004).
1.2 Statement of the Problem

Over the past decades, fundamental changes in the industry of financial intermediation, such as deregulation and advances in technology, had a visible impact on the provision of financial services. Deregulation, in various parts of the world, has made flexible the provision of financial services and promoted competition among financial institutions. In Kenya, this has seen the entry of Mobile telecommunication companies into banking industry thus limiting commercial banks revenues substantially (Berger, 2003 and Berger and DeYoung, 2006). One of the most prominent transformations undergone by the financial services industry has been the emergence and expansion of bancassurance (or bank-insurance).

In present global economy, integration and strategic alliance are omnipresent. Few studies have examined the effects of the diversification achieved by banking and insurance company mergers per se. The literature examining the most suitable models of such bancassurance alliance models is limited. As discussed by Boyd, Graham, and Hewitt (1993), numerous studies have attempted to determine the potential effects of expansion of bank holding companies into permissible nonbank activities and prohibited nonbank activities. However, these studies investigate different financial services firms separate from one another, rather than merger combinations of banks and nonbank firms. Further, there is controversy on the effect of the merger on profitability with some researchers concluding that there is a positive effect (Staikouras and Nurullah, 2008) while Korhonen and Voutilainen (2006) find a negative effect on performance.

Further, as outlined in Chen et al. (2009), most studies dealing with bancassurance have only been descriptive in nature, providing a broad insight into economic rationales, advantages and drawbacks for all the institutions involved. Only few authors have provided quantitative findings, focusing on the potential risk diversification benefits associated with bank expansion into the insurance industry (Laderman, 2000). Nevertheless risk reduction is not universally recognized as a valid economic rationale for diversification: one may observe that shareholders can always reduce their risk by holding a diversified portfolio of non diversified firms, gaining the risk-reduction advantages of diversification without incurring in the costs of managing a large and complex organization (Klein and Saidenberg, 2000). Thus diversification would be worth only if it provides some kind of cost or revenues economies, improving the operational efficiency of financial firms.
Despite the importance of this issue, few empirical analyses have directly assessed efficiency issues in the bancassurance business and, as far as the researcher is aware, none of these focused on performance differences among alternative forms of cooperation between the banking and the insurance industries. This is despite the fact that most of the commercial banks in Kenya are adopting bancassurance services without any tangible effect on their financial performance. At present most of the insurance companies have product information and/or illustrative tools on the web. In the Kenyan market, where insurance is sold after considerable persuasion even after face-to-face selling, the selling over the net, which must be initiated by the client, would take some more time.

Locally, Wachira (2012) investigated the factors influencing customer’s adoption of bancassurance channel of insurance distribution in Nairobi Central Business District. To the best of the researcher’s knowledge, no study has been done on the effect of bancassurance on financial performance of commercial banking industry in Kenya. This study therefore seeks to fill this knowledge gap by investigating the effect of bancassurance on financial performance of commercial banking industry in Kenya.

1.3 Objectives of the Study

1.3.1 General Objective

The general objective of this study was to establish the effect of bancassurance on financial performance of commercial banking industry in Kenya.

1.3.2 Specific Objectives

The specific objectives of this study were:

i. To establish the level of bancassurance adoption among commercial banks in Kenya

ii. To investigate the effect of bancassurance on financial performance of commercial banks in Kenya
1.4 Significance of the Study

The findings of this study will be invaluable to various stakeholders including the commercial banks in Kenya, The Government, the Central Bank of Kenya (CBK) and scholars.

Commercial banks in Kenya and other financial intuitions will benefit from the findings of this study on the effect of bancassurance on financial performance. The study will also provide insights into the bank – insurance model as a viable business strategy for enhancing the performance, thus, influence decision making. The management of the firms will be enlightened to understand if their strategies are reaching the desired objectives and what the financial institutions needs putting in place to safeguard their existence.

The government and CBK would find useful information that would help them in formulation of policies that will lead to more profitable firms. This is because as the financial sector grows the government has to come up with policies that address the various challenges within the sector so as to facilitate faster growth with minimum drawbacks.

This area of effect of bancassurance on financial performance is still suffering from a lack of information. Research in the various components in this area would help to unearth hitherto unknown information that would go a long way in facilitating further understanding of the effect of bancassurance on financial performance. It will also contribute to the existing body of knowledge and fill in the gap on the effect of bancassurance on financial performance. It would also act as a source of reference materials to scholars.
CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter summarizes the information from other researchers who have carried out their research in the same field of study. The specific areas covered here are theoretical review, empirical review, conceptualization, the critical review and the gap.

2.2 Theoretical Review

This section covers the theoretical underpinnings guiding this study by looking at the modern portfolio theory (MPT) and classic finance theory.

2.2.1 Modern Portfolio Theory (MPT)

Modern portfolio theory (MPT) is a theory of finance which attempts to maximize portfolio expected return for a given amount of portfolio risk, or equivalently minimize risk for a given level of expected return, by carefully choosing the proportions of various assets. MPT is a mathematical formulation of the concept of diversification in investing, with the aim of selecting a collection of investment assets that has collectively lower risk than any individual asset. That this is possible can be seen intuitively because different types of assets often change in value in opposite ways (Markowitz, 1959).

But diversification lowers risk even if assets' returns are not negatively correlated—indeed, even if they are positively correlated. More technically, MPT models an asset's return as a normally distributed function (or more generally as an elliptically distributed random variable), defines risk as the standard deviation of return, and models a portfolio as a weighted combination of assets, so that the return of a portfolio is the weighted combination of the assets' returns (Sabbadini, 2010). By combining different assets whose returns are not perfectly positively correlated, MPT seeks to reduce the total variance of the portfolio return. MPT also assumes that investors are rational and markets are efficient.

An investor can reduce portfolio risk simply by holding combinations of instruments which are not perfectly positively correlated. In other words, investors can reduce their exposure to
individual asset risk by holding a diversified portfolio of assets. Diversification may allow for the same portfolio expected return with reduced risk (Koponen, 2003). The fundamental concept behind MPT is that the assets in an investment portfolio should not be selected individually, each on their own merits. Rather, it is important to consider how each asset changes in price relative to how every other asset in the portfolio changes in price.

With regard to loan portfolio diversification, we also record different results across banking groups from the two-stage least squares regressions. According to portfolio theory returns should be more volatile for banks with specialized loan portfolios; well capitalized banks and banks with less risky loan portfolios enjoy more stable returns. Consistent with portfolio theory, an increased reliance on non-interest income is associated with higher volatility of returns, but a more highly diversified revenue portfolio is associated with lower volatility. While returns from non-interest bearing activities tend to be less stable than those from interest bearing activities, there is also a diversification benefit in the form of reduced volatility for banks with a higher share of non-interest income in total income (Koponen, 2003).

2.2.2 Classic Finance Theory

Classic finance theory suggests that firms should not expend resources on risk-reduction because an investor could diversify by buying a wide-range of securities (Berger et al., 2001). Finance theory suggests that firms should not utilize valuable resources to reduce risk because equity market investors can diversify and shed idiosyncratic (firm-specific) risk themselves by holding a well-diversified portfolio of stocks. This view is appropriate for banks due to financial market imperfections, agency costs, and informational asymmetries, so the total risk of banks, which is proxied by the unconditional volatility of profits, provides relevant and useful information. Moreover, total risk and volatility are important concerns of other stakeholders including regulators/supervisors, management, and borrowers.

From the regulator/ supervisor perspective, there is a clear concern with the costs associated with failure, e.g., transaction and liquidation costs related to bankruptcy, systemic risk concerns, and costs to the insurance fund. As a result, supervisory interest is not in a market portfolio of diversified stocks, but rather in the total risk of the individual institutions that it supervises. This can be seen directly in Merton-type portfolio models of credit risk, developed by Merton (1974).
and implemented in risk models, which are driven by assumptions about total asset return volatility.

2.3 Empirical Review

There are many potential benefits to be realized by bancassurance strategies. It has to be urged that potential refers to the opportunities of bancassurance. Those opportunities do not always necessarily work out well. The analysis of the bancassurance phenomenon can be made focusing either the banking or the insurance standpoint. Adopting the banking point of view, we can find only a handful of studies dealing specifically with efficiency gains from diversification (Casu and Girardone, 2004). It is worthwhile to emphasize that all these studies adopt a definition of banking diversification different from the concept of bancassurance. Allen and Rai (1996) examine cost efficiency of banks during the period 1988-1992 for a sample of 15 different countries allowing or not the integration between traditional and investment banking. Vander Vennet (2002) measures cost and profit efficiency in European banks in 1995-1996, showing that financial conglomerates, defined as combinations between commercial banking and investment banking or insurance, are more revenue efficient than specialised banks. Casu and Girardone (2004) find an increase in profit efficiency of financial conglomerates, defined as all Italian banking groups, supposing that they generally experienced a trend towards conglomeration during the observed period (1996-1999).

Berger and Ofek (1995) find that diversified firms have values that are 13-15 percent below the sum of the imputed values of their segments, but this loss is mitigated in cases of more focused diversification within related industries. Diversification can enhance value through increased cash flow and/or through reduced risk. Therefore, merger studies assess the impact of mergers on stock returns of the bidder (which could imply improved future cash flows or anticipated risk reduction or both) or on the risk changes experienced by the bidding firm. The focus of the few studies that do examine bancassurance (unlike in the corporate finance literature) is principally on changes in risk. An exception is Fields, Fraser, and Kolari (2007), who find that bidders in bancassurance mergers experience positive wealth effects and that these wealth effects appear to be driven by enhanced economies of scale and scope and by geographic diversification.
Cybo-Ottone and Murgia (2000) examined the shareholder wealth effects of 54 large European bank mergers (exceeding $100 million) but found only 10 banking-insurance mergers with publicly traded stock price data for both buyer and seller and, of these, only 8 were completed. Consistent with most merger studies, targets experienced wealth gains, whereas acquirers had no significant changes in their share prices around merger announcement dates in the period 1988 through 1997. These small sample sizes make it difficult to draw meaningful inferences about the wealth effects of bancassurance or the potential sources of gains.

According to Estrella (2001), there are advantages of risk diversification that can be realised from implementing the bancassurance strategy. Insurers face a specific risk profile that differs from operators in the market for traditional banking services. In fact, a traditional wisdom is that one should not put all the eggs in the same basket. Hence insurances can be a matter of risk diversification as well. Estrella (2001) found risk reduction for commercial banks that engage in non-traditional banking activities. It should be noted though, that this risk reduction might be part of the increased size of a bank. In the end, like observed during the recent financial crisis, some ‘systemic’ banks are regarded to be too big to fail and were saved from bankruptcy by national authorities.

Chen et al (2009) found valid grounds for economies of scope based on observed close similarities (e.g. financial risk management, liquidity creation) between banks and insurers. They noticed in the same year that once banks have established a customer contact for one service, they could leverage this contact with small incremental costs to sell additional services. This is a clear example of potential economies of scope that are often put forward by responsible managers. Economies of scope arise from similarities that may occur among the assets that are in place to run the business.

Basically, the more insurance products a bank (branch) sells, the more experience it will gain along with scale advantages, and ultimately the marginal selling costs can decrease. A research by Staikouras (2006) showed that banking and insurance businesses have more commonalities than differences. Thus, this study supports motivations to attain economies of scope and economies of scale, which can be converted in cost reductions. Both categories of cost effectiveness put banks in an advantageous position compared to brokers and (tied) agents.
Berger (2001) observed that it is very simple to understand how similar synergies can be realised in bancassurance combinations or in other diversified financial firms. From the cost side, we can think to the opportunity of: sharing physical inputs (like offices or computers), staff costs and distribution net; employing common information systems, investment departments, account service centres; reusing managerial expertise or information; obtaining capital with larger issue size.

Berger (2001) point out as scope economies can arise also from the revenue side. The idea is that consumer could be willing to pay higher prices for one stop banking, because of reductions in user transaction and search cost associated with consuming different financial services offered by the same provider, often at the same location. But in their empirical analysis, they do not find evidence of revenue scope economies between deposits and loans, over 1978-1990, for both small and large banks. In their opinion, this result for the provision of current banking services, where benefits are most likely to occur if they occur at all, is suggestive of similarly small synergies from an expansion of banking powers into new service areas.

Allen and Rai (1996) examine cost efficiency of banks during the period 1988-1992, for a sample of 15 different countries. They examine two groups of countries: universal banking countries that allow the integration between traditional and investment banking and separated banking countries that do not. The authors also account for size effects, finding that large banks in separated banking countries have the largest measure of input inefficiency.

Vander (2002) used a parametric methodology in order to measure cost and profit efficiency in European banks in 1995-1996: his results show that financial conglomerates are more revenue efficient than specialized banks and that universal banks are more efficient on both the cost and revenue sides. Casu and Girardone (2004) used both statistical and mathematical approaches to measure the efficiency of Italian financial conglomerates between 1996 and 1999 and find evidence of an increase in profit efficiency.

Ward and Zurbruegg (2002) investigated the determinants of consumption in Asia (22 countries). They compared their panel with OECD countries. Analyzing the data from 1987 through 1998, they found evidence that improved civil rights and political stability leads to an increase in the consumption of life insurance in the Asian countries as well as in OECD region.
Ely and Robinson (2001) further elaborated on the transformation of banking. They argue that the functional view of the financial system will provide a valuable framework to understand how the future of financial institutions might evolve. The point of departure is the underlying functions that all financial systems must provide, in order to make an economic system work.

Estrella (2001) also found that both banks and insurers can experience diversification benefits when convergence materializes. He suggests that life/non-life insurance is risk reducing, he also finds (contrary to the above) that securities underwriting reduces the probability of bankruptcy. Further, Kist (2001) studied the synergies that can be achieved by integrating insurance, banking and asset management under one provider of financial services. He analyses the dynamics of profitability and identifies five key factors that are crucial for its success i.e. customer base, available branches, insurance specialists per branch, staff knowledge, and the cross-selling ratio.

2.4 Conclusion

From the review of existing empirical literature, we can conclude that even if improving efficiency through cost and revenue synergies is probably the most valid rationale for banking diversification into the insurance industry, potential efficiency gains in bancassurance are still less explored than other topics, like risk reduction benefits. So it could be interesting to provide new evidence on this key issue, with a particular focus on European countries.

In order to have a complete view of the bancassurance phenomenon, a comprehensive study should adopt both the banking and the insurance points of view, but differences in the type of business and financial reporting models may cause problems of comparability. A possible solution to account for these differences and still assess bancassurance efficiency gains from both sides is to conduct two separated analyses, one in the banking sector and one in the insurance sector.

Much has been done on general diversification strategies. An ongoing debate is centralized on whether diversified firms outperform specialized counterparts. One can observe a certain disagreement for the questioned outperformance of diversifiers in general. Carter (1977) and Grant & Jammie (1988) first found value creation in diversification. Later on, Berger &Ofek (1995) and Lang &Stulz (1994) contributed to the debate on bancassurance by showing
contradictive results. Lloyd & Jahera (1994) added ambiguity revealing no significant effects on value creation of diversified versus specialized firms. Obviously, reason for his can be found in the existence of alternative data and methodologies for diversification- and performance measurement. Datta et al. (1991) cleared up complexity in a general framework with key variables for fruitful diversification strategies.

Locally, Karanja (2012) did a study on the effects of income source diversification on financial performance of commercial banks in Kenya a case of Equity Bank while Mwangi (2010) did a study on the implementation of diversification strategy at the Standard Group (K) Limited. None of the studies focused on the effect of bancassurance. Potential efficiency gains from bancassurance combinations are still a poorly investigated issue, even if cost and revenue synergies are commonly recognized as the most valid rationale for banking diversification into other sectors of financial intermediation.
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction

This chapter sets out various stages and phases that were followed in completing the study. It involves a blueprint for the collection, measurement and analysis of data. In this stage, most decisions about how research was executed and how respondents were approached, as well as when, where and how the research was completed. Therefore in this section the research identified the procedures and techniques that were used in the collection, processing and analysis of data. Specifically the following subsections were included; research design, target population, sampling design, data collection procedures and finally data analysis.

3.2 Research Design

Research design refers to the way the study is designed, that is, the method used to carry out a research. Orodho (2003) defines a research design as the scheme, outline or plan that is used to generate answers to research problems. This study was a descriptive survey. Descriptive survey was preferred for it is used to obtain information concerning the current status of a phenomenon. The method was chosen since it is more precise and accurate since it involves description of events in a carefully planned way (Babbie, 2004).The purpose of this method is to describe what exists with respect to situational variables i.e. it looks at relationship between and among variables (Mugenda and Mugenda, 2003).

3.3 Target Population

Target population in statistics is the specific population about which information is desired (Ngechu, 2004). The target population of this study was the nine commercial banks in Kenya that have taken up bancassurance. Mugenda and Mugenda, (1999), explain that the target population should have some observable characteristics, to which the researcher intends to generalize the results of the study.
3.4 Sampling Procedures

Ngechu (2004) underscores the importance of selecting a representative sample through making a sampling frame. From the population frame the required number of firms was selected in order to make a sample. Due to the population size of commercial banks in Kenya that have taken up bancassurance, the research took the census approach. A census is where data is collected from all members of the population (Hair, Celsi, Money, Samouel, & Page, 2011).

3.5 Data Collection

Secondary data collection method was used in this study. The secondary data was collected from the commercial banks audited financial statements and also CBK for the year 2008-2012.

3.6 Data Analysis Methods

Data was analyzed using Statistical Package for Social Sciences (SPSS Version 21.0) program. Being that the study was descriptive in nature, both quantitative analysis and inferential analysis was used as data analysis technique. The data collected was run through various models so as to clearly bring out the effects of bancassurance on bank financial performance. The results obtained from the models were presented in tables to aid in the analysis and ease with which the inferential statistics was drawn. The under-mentioned model was used:

\[ Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon \]

Where:
- \( Y \) = Financial performance of commercial banks (ROE)
- \( \beta_0 \) = Constant Term
- \( \beta_1, \beta_2 \) and \( \beta_3, \beta_4 \) = Beta coefficients
- \( X_1 \) = Bancassurance (Total volume premium covers in KShs)
- \( X_2 \) = Inflation (Consumer price indexes)
- \( X_3 \) = GDP
- \( X_4 \) = Size
- \( \varepsilon \) = Error term
CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction
This chapter presents the information processed from the data collected during the study on effects of bancassurance on financial performance of commercial banks in Kenya. The sample composed of nine commercial banks in Kenya that have taken up bancassurance for the period (2008-2012).

4.2 Regression Results
The study conducted a multiple regression on the selected independent variables over the period 2008–2012 and financial performance of commercial banks.

4.2.1 Year 2008 Analysis and Interpretations
Coefficient of determination explains the extent to which changes in the dependent variable can be explained by the change in the independent variables or the percentage of variation in the dependent variable (Financial performance of commercial banks) that is explained by the four independent variables (Bancassurance, size of the bank, inflation and GDP).

**Table 4.1: ANOVA Statistics for 2008 Data**

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.999&lt;sup&gt;a&lt;/sup&gt;</td>
<td>.999</td>
<td>.994</td>
<td>152.75012</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>2.164E7</td>
<td>4</td>
<td>4328509.766</td>
<td>185.513</td>
<td>.046&lt;sup&gt;a&lt;/sup&gt;</td>
</tr>
<tr>
<td>Residual</td>
<td>23332.599</td>
<td>1</td>
<td>23332.599</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>2.167E7</td>
<td>5</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Table 4.2: Coefficients of 2008 Model

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>-1802.653</td>
<td>2125.285</td>
<td>-.848</td>
<td>.552</td>
</tr>
<tr>
<td>Bancassurance</td>
<td>.205</td>
<td>.000</td>
<td>.091</td>
<td>1.935</td>
</tr>
<tr>
<td>Size</td>
<td>.013</td>
<td>.004</td>
<td>.356</td>
<td>3.610</td>
</tr>
<tr>
<td>Inflation</td>
<td>176.053</td>
<td>140.868</td>
<td>.065</td>
<td>1.250</td>
</tr>
<tr>
<td>GDP</td>
<td>-1239.903</td>
<td>615.149</td>
<td>-.170</td>
<td>-2.016</td>
</tr>
</tbody>
</table>

The data findings from 2008 market statistics were analyzed and the SPSS output presented in table 1 and 2 above. From the ANOVA statistics in table 1, the processed data, which are the population parameters, had a significance level of 0.046 which shows that the data is ideal for making a conclusion on the population’s parameter. The coefficient table in table 2 above was used in coming up with the model below:

\[
FP = -1802.653 + 0.205 \text{Bancassurance} + 0.013 \text{Size} + 176.053 \text{Inflation} - 1239.903 \text{GDP}
\]

According to the model, only GDP was negatively correlated with financial performance of commercial banks while bancassurance, inflation and size of the bank were positively correlated with financial performance of commercial banks. From the model, taking all factors (bancassurance, size of the bank, inflation and GDP) constant at zero, financial performance of commercial banks will be \(-1802.653\). The data findings analyzed also shows that taking all other independent variables at zero, a unit increase in bancassurance will lead to a \(0.205\) increase in financial performance of commercial banks. A unit increase in size of the bank will lead to a \(0.013\) increase in financial performance of commercial banks; a unit increase in inflation will lead to a \(176.053\) increase in financial performance of commercial banks while a unit increase in GDP will lead to a \(-1239.903\) decrease in financial performance of commercial banks. This infers that bancassurance had a positive effect on financial performance of commercial banks.
4.2.2 Year 2009 Analysis and Interpretations

Table 4.3: ANOVA Statistics for 2009 Data

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.999(^a)</td>
<td>.998</td>
<td>.988</td>
<td>248.75242</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>3.004E7</td>
<td>4</td>
<td>6008288.047</td>
<td>97.099</td>
<td>.027(^a)</td>
</tr>
<tr>
<td>Residual</td>
<td>61877.767</td>
<td>1</td>
<td>61877.767</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>3.010E7</td>
<td>5</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 4.4: Coefficients for 2009 Regression Model

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>-613.247</td>
</tr>
<tr>
<td></td>
<td>Bancassurance</td>
<td>-9.875E-5</td>
</tr>
<tr>
<td></td>
<td>Size</td>
<td>.003</td>
</tr>
<tr>
<td></td>
<td>Inflation</td>
<td>-0.5538</td>
</tr>
<tr>
<td></td>
<td>GDP</td>
<td>153.639</td>
</tr>
</tbody>
</table>
The data findings for 2009 statistics were processed using SPSS and the output presented in table 3 and 4 above. According to the ANOVA table 3 above, the parameters predicted in the table above had a significance level of 0.027 which is inadequate to be used as a population parameter in predicting the effect of bancassurance on financial performance of commercial banks. The regression model drawn from table 4 above is presented below:

$$FP = -613.247 + 0.003\text{Banc} + 0.5538\text{SIZ} - 0.5538\text{INF} + 153.639\text{GDP}$$

According to the table, the financial performance of commercial banks had an autonomous value of -613.247 that is when the value of all the independent variables is zero. A unit increase in bancassurance decreases the financial performance of commercial banks by -9.875E-5 when the inflation, GDP and size of the bank variables are held constant. A unit increase in size of the bank, holding other variables constant, increased the financial performance of commercial banks by 0.003. A unit increase in inflation, holding other variables constant, decreased the financial performance of commercial banks by -0.5538 while a unit increase in GDP, holding other variables constant, increased the financial performance of commercial banks by 153.639. This shows that Size and GDP had a positive relationship with the financial performance of commercial banks with bancassurance and inflation having a negative effect on financial performance of commercial banks.

4.2.3 Year 2010 Analysis and Interpretations

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1.000\textsuperscript{a}</td>
<td>1.000</td>
<td>.997</td>
<td>219.73203</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression</td>
<td>9.667E7</td>
<td>4</td>
<td>1.933E7</td>
<td>400.453</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>48282.166</td>
<td>1</td>
<td>48282.166</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>9.672E7</td>
<td>5</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Table 4.6: 2010 Model Coefficients

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>14447.430</td>
<td>3156.316</td>
<td>4.577</td>
</tr>
<tr>
<td></td>
<td>Bancassurance</td>
<td>.1005</td>
<td>.000</td>
<td>.153</td>
</tr>
<tr>
<td></td>
<td>Size</td>
<td>.018</td>
<td>.005</td>
<td>-.318</td>
</tr>
<tr>
<td></td>
<td>Inflation</td>
<td>-40.994</td>
<td>87.894</td>
<td>-.022</td>
</tr>
<tr>
<td></td>
<td>GDP</td>
<td>2562.183</td>
<td>622.000</td>
<td>.249</td>
</tr>
</tbody>
</table>

From the finding of the study on the 2010 market statistics as analyzed and presented in the above table, the following regression equation was established by the study for the year 2010:

\[
FP = 14447.430 + 0.3005 \text{ Banc} + 0.018 \text{ SIZ} - 40.994 \text{ INF} + 2562.183 \text{ GDP}
\]

From the findings of the data it can be concluded that when the value of bancassurance, inflation, GDP and size of the bank were zero, financial performance of commercial banks was 14447.430. The table also shows that holding inflation, GDP and size of the bank constant, an increase by one unit of bancassurance increases financial performance of commercial banks by 0.1005, when other factors are held constant an increase in size of the bank by one unit increases financial performance of commercial banks by 0.018. If one unit of inflation was increased while holding other factors constant, the financial performance of commercial banks would decrease by -40.994 while a unit increase in GDP will increase the financial performance of commercial banks by 2562.183 holding other factors constant. This shows that the bancassurance, size and GDP have a positive relationship with financial performance of commercial banks while inflation inversely affects financial performance of commercial banks, although the GDP influences financial performance of commercial banks positively most.
Moreover, the model was arrived at a significance level of 0.038 which means that the model is adequate in drawing a conclusion on the population parameters.

### 4. 2.4 Year 2011 Analysis and Interpretations

**Table 4.7: ANOVA statistics for 2011 Model**

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.999&lt;sup&gt;a&lt;/sup&gt;</td>
<td>.999</td>
<td>.992</td>
<td>446.99774</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression</td>
<td>1.582E8</td>
<td>4</td>
<td>3.165E7</td>
<td>158.383</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>199806.978</td>
<td>1</td>
<td>199806.978</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>1.584E8</td>
<td>5</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Table 4.8: Coefficients of model 2011**

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 (Constant)</td>
<td>-1290.475</td>
<td>2991.614</td>
<td>-.431</td>
<td>.741</td>
</tr>
<tr>
<td>Bancassurance</td>
<td>1.337E-5</td>
<td>.000</td>
<td>.005</td>
<td>.100</td>
</tr>
<tr>
<td>Size</td>
<td>.022</td>
<td>.009</td>
<td>.361</td>
<td>2.326</td>
</tr>
<tr>
<td>Inflation</td>
<td>-443.432</td>
<td>457.845</td>
<td>-.036</td>
<td>-.969</td>
</tr>
<tr>
<td>GDP</td>
<td>676.212</td>
<td>477.902</td>
<td>.073</td>
<td>1.415</td>
</tr>
</tbody>
</table>

The market data for 2011 was regressed on SPSS and the output presented in table 7 and 8 above. From the data analyzed and presented in the table above, the model for the year 2011 is presented below:
FP = -1290.475 + 1.337E-5 Banc + 0.022 SIZ -443.432INF + 676.212 GDP

According to the model above, holding bancassurance, size of the bank, inflation and GDP constant at zero, financial performance of commercial banks will be -1290.475. When the inflation, GDP and size of the bank are held constant, a unit increase in bancassurance will increase the financial performance of commercial banks by 1.337E-5. When other factors are held constant, a unit increase in size of the bank will increase the financial performance of commercial banks by 0.022. The model also shows that inflation had a negative relationship with financial performance of commercial banks such that a unit increases in inflation holding other factors constant will lead to a decrease in financial performance of commercial banks by -443.432. A unit increase in GDP will increase the financial performance of commercial banks by 676.212 holding other factors constant.

From the above model it can be concluded that bancassurance, size of the bank, and GDP positively influenced financial performance of commercial banks. From the ANOVA statistics table 7 above, it shows that the parameters in the model have a 0.036 level of significance which shows that it is significant in predicting the effect of bancassurance on financial performance of commercial banks.

4.2.5 Year 2012 Analysis and Interpretations

Table 4.9: ANOVA Statistics for 2012

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.969a</td>
<td>.938</td>
<td>.629</td>
<td>3205.77012</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Regression</td>
<td>1.561E8</td>
<td>4</td>
<td>3.121E7</td>
<td>3.037</td>
<td>.0409a</td>
</tr>
<tr>
<td>Residual</td>
<td>1.028E7</td>
<td>1</td>
<td>1.028E7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1.663E8</td>
<td>5</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Table 4.10: Coefficients of model 2012

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 (Constant)</td>
<td>-7270.078</td>
<td>14627.521</td>
<td>-.497</td>
<td>.706</td>
</tr>
<tr>
<td>Bancassurance</td>
<td>.001</td>
<td>.002</td>
<td>.586</td>
<td>.870</td>
</tr>
<tr>
<td>Size</td>
<td>.038</td>
<td>.050</td>
<td>.714</td>
<td>.746</td>
</tr>
<tr>
<td>Inflation</td>
<td>-563.999</td>
<td>811.773</td>
<td>-.352</td>
<td>-.695</td>
</tr>
<tr>
<td>GDP</td>
<td>2868.035</td>
<td>3859.063</td>
<td>.371</td>
<td>.743</td>
</tr>
</tbody>
</table>

The data findings for 2012 were computed, analyzed and presented in table 9 and 10 above. According to the ANOVA statistics in table 9 above, the model had a significance level of 0.0409 which means that the model is appropriate to be used as a population parameter. From table 10, the regression model is presented below:

\[
FP = -7270.078 + 0.001 \text{Banc} + 0.038 \text{SIZ} - 563.999 \text{INF} + 2868.035 \text{GDP}
\]

According to the regression model, when the values of bancassurance, size of the bank, inflation and GDP are zero, financial performance of commercial banks will be -7270.078. When bancassurance is increased by one unit, the financial performance of commercial banks will decrease by 0.001 while when size of the bank is increased by one unit, the financial performance of commercial banks will increase by 0.038. The financial performance of commercial banks will also decrease by -563.999 when the inflation is increased by one unit holding other factors constant. This shows that in this year, size of the bank, bancassurance and GDP had a positive correlation with financial performance of commercial banks while inflation had a negative effect on the same.

**4.3 Summary and Interpretation of Findings**

From the above regression models for the five years, the study found out that there were several factors influencing the financial performance of commercial banks in Kenya, which are
bancassurance, size of the bank, inflation and GDP. They either influenced it positively or negatively. The study found out that the intercept varied. The highest value was 14,447.43 and the lowest was -7,270.08) with an average of 694.20 for all years. The study also found out that the coefficient of bancassurance varied from positive to negative. The highest regression value was positive with an average coefficient of 0.101282924. This means that bancassurance positively influenced the financial performance of commercial banks.

The study found out that the size of the bank varied in value although it was positive all cases. This means that size of the bank positively influenced the financial performance of commercial banks. The study further found out that the coefficients of the inflation to be negative in four out of the five regression models. This depicts that, according to findings, inflation negatively influences the financial performance of commercial banks.

The four independent variables that were studied (Bancassurance, size of the bank, inflation and GDP) explain only 98.68% of financial performance of commercial banks as represented by the average $R^2$ (0.9868). This therefore means the four independent variables only contribute about 98.68% of financial performance of commercial banks decision while other factors not studied in this research contributes 1.32% of the financial performance of commercial banks.

There have been several studies carried out on the effect of bancassurance but findings have to a large extent corroborated the findings on the effect of bancassurance on financial performance of commercial banks in Kenya. The study concludes that bancassurance have a weak positive influence on the financial performance of commercial banks in Kenya. My results are consistent with prior research by Staikouras and Nurullah (2008) who indicated that banks are now major distribution channels for insurers and insurance sales have formed a significant source of profits for banks. According to Kirui (2009), Banking institutions and insurance companies have found bancassurance to be an attractive and profitable complement to their existing business activities.

The findings are also consistent with a recent study on bancassurance where Fields, Fraser and Kolari (2012) found that bancassurance deals lead to a win-win situation for both bidder-target firms in the US. At the same time, a banking study by Cybo-Ottone and Murgia (2010) reported that European M&A lead to a positive and significant increase in stock market value for the average merger at the time of the deal announcement.
The study deduced that although the overall relationship between bancassurance and financial performance of commercial banks is positive, there are some cases showing negative relationship. Thus, the relationship between bancassurance and financial performance of commercial banks remains a controversial. This is in line with earlier studies that showed mixed results about the relationship between bancassurance and financial performance of commercial banks. Thus, there is controversy on the effect of the merger on profitability with some researchers concluding that there is a positive effect (Staikouras and Nurullah, 2008) while Korhonen and Voutilainen (2006) find a negative effect on performance.

From the findings, it can be observed that bancassurance affect financial performance of commercial banks positively. Any time bancassurance increases the income to the banks inform of commission increases. However, the study deduced that the dummy variables, size of the bank and GDP positively influence financial performance of commercial banks hence the conclusion of this study is that bancassurance, size of the bank and GDP have strong positive correlation with financial performance of commercial banks while inflation have strong and negative correlation with financial performance of commercial banks. Therefore it will be important for a bank management to understand the relationship that exists between bancassurance, size of the bank, GDP, inflation and financial performance of commercial banks and the direction that they affect the level of financial performance of commercial banks for suitable policy making.
CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The secondary data in this analysis covered a period of 5 years from 2008 to 2012. The population of study comprised of nine commercial banks in Kenya that have taken up bancassurance for the period (2008-2012). The purpose of the study is to investigate the effect of bancassurance on financial performance of commercial banks in Kenya.

This study was conducted through the use of a descriptive design. The study used purposeful sampling to pick nine commercial banks in Kenya that have taken up bancassurance for the period (2008-2012) which was exposed to sensitivity analysis using OLS regression.

The study found that the regression equations for the period 2008 to 2012 related financial performance of commercial banks to the bancassurance, size of the bank, inflation and GDP. From the above regression models for the five years, the study found out that there were several factors influencing the financial performance of commercial banks, which are bancassurance, size of the bank, inflation and GDP. They either influenced it positively or negatively. The four independent variables that were studied (Bancassurance, size of the bank, inflation and GDP) explain only 98.68% of financial performance of commercial banks as represented by the average $R^2$ (0.9868). The study concludes that bancassurance have a weak positive but significant influence on the financial performance of commercial banks in Kenya. The study recommends that the study recommends that the bank managers should promote the adoption of the bancassurance to their customers through advertising to its customers most of whom are not insured. Intense market competition between banks has led to a substantial decrease in the interest margins of the traditional banking products. Banks should take advantage of widespread branch network across the country in the distribution of insurance products. Banks should seek to offset some of the losses by entering life insurance business. Life insurance is also frequently supported by favorable tax treatment to encourage private provision for protection or retirement planning. This preferential treatment makes insurance products more attractive to customers and banks should see an opportunity for profitable sales of such products.
5.2 Conclusions

This paper examines the effect of bancassurance on financial performance of commercial banks in Kenya. The study concludes that bancassurance have a weak positive influence on the financial performance of commercial banks in Kenya. The banking and insurance industry have changed rapidly in the changing and challenging economic environment throughout the world. In the competitive and liberalized environment everyone is trying to do better than others and consequently survival of the fittest has come into effect. Intense competition between banks, against a background of shrinking interest margins, has led to an increase in the administrative and marketing costs and limited the profit margins of the traditional banking products. New products could substantially enhance the profitability and increase productivity. The distribution of insurance products through a bank’s distribution channel brings diversification advantages by generating non-interest related income. The bancassurance model could eventually create cross-selling business synergies for banks that in turn can lead to cost savings through economies of scope. Basically, the more insurance products a bank (branch) sells, the more experience it will gain along with scale advantages, and ultimately the marginal selling costs can decrease.

The bancassurance effect on financial performance mainly result from increased income generated, in the form of commissions and/or profits from the business (depending upon the relationship), reduction of the effect of the bank’s fixed costs, as they are now also spread over the life insurance relationship, opportunity to increase the productivity of staff, as they now have the chance to offer a wider range of services to clients and banks can cross sell insurance products e.g. term insurance products with loans.

The study deduced that although the overall relationship between bancassurance and financial performance of commercial banks is weak and positive, there are some cases showing negative relationship. Thus, the relationship between bancassurance and financial performance of commercial banks remains a controversial. This show there is mixed results about the relationship between bancassurance and financial performance of commercial banks with both a negative relationship and a positive relationship between bancassurance and financial performance of commercial banks. This also point on the existence of a non linear relationship between these two variables and supports the hypothesis that higher amounts of bancassurance
promotes financial performance of commercial banks while low level bancassurance have significantly negative effect on financial performance of commercial banks.

5.3 Recommendations for Policy and Practice
Since the study established that bancassurance has a significant influence on the financial performance of commercial banks, the study recommends that the bank managers should promote the adoption of the bancassurance to their customers through advertising to its customers most of whom are not insured. Intense market competition between banks has led to a substantial decrease in the interest margins of the traditional banking products. Commission and fees from the selling of insurance products will supplement their earnings. Banks should take advantage of widespread branch network across the country in the distribution of insurance products.

Customer preferences regarding investments are changing. For medium-term and long-term investments there is a trend away from deposits and toward insurance products and mutual funds where the return is usually higher than the return on traditional deposit accounts. This shift in investment preferences has led to a reduction in the share of personal savings held as deposits, traditionally the core element of profitability for a bank which manages clients’ money. Banks should seek to offset some of the losses by entering life insurance business. Life insurance is also frequently supported by favourable tax treatment to encourage private provision for protection or retirement planning. This preferential treatment makes insurance products more attractive to customers and banks should see an opportunity for profitable sales of such products.

The high operating expenses of bank branches have led many banks to decrease their branch network. The need for more efficient utilization of branches and bank employees is today as pressing as ever. There is thus the need to utilize the branches and bank staff more efficiently and making them as profit centers and bancassurance can boost this. Banks should also use this as an opportunity to increase the productivity of staff since they now have the chance to offer a wider range of products and services to clients.

Banks are experiencing the increased mobility of their customers, who to a great extent tend to have accounts with more than one bank. Therefore there is a strong need for customer loyalty to an organization to be enhanced. Client relationship management should be used as a key
strategy. To build and maintain client relationships, banks and insurers should form partnerships to provide their clients with a wide range of bank and insurance products from one source. It is believed that as the number of products that a customer purchases from an organization increases the chance of losing that specific customer to a competitor decreases.

Banks have witnessed a decline in margins in their core lending business due to falling interest rates. Insurance distribution helps to increase the fee based earnings of banks to a considerable extent. So the bank employees should try to increase the total other income of the bank by doing cross selling. The bank employees who are involved in bancassurance should be given full knowledge of the target customers. In order to attract more policy holders, the bank employees and insurance agents should promptly attend to the enquiries of policyholders. Further, bank should try to facilitate online and internet payments towards insurance products.

5.4 Limitations of the Study

Every live and non-live factor has its own limitations which affect the usability of that factor. The same rule applies to this research work. This study was mainly based on secondary data derived from the annual reports of the bank. The reliability and the findings are contingent upon the data published in the annual reports.

Financial analysis does not depict those facts which cannot be expressed in terms of money, for example efficiency of workers, reputation and prestige of the management, etc which also affect the financial performance.

Further, the model may not be reliable due to some shortcoming of the regression models. Due to the shortcomings of regression models, other models can be used to explain the various relationships between the variables.

Financial ratios have their own limitations which applied in this study. Further, the data was tedious to collect and compute as it was in very raw form.

5.5 Suggestions for Further Research

This paper examines the effect of bancassurance on financial performance of commercial banks in Kenya. Because of data unavailability, it was not possible to include all the banks in our
sample. Therefore I suggest further research on the effect of bancassurance on financial performance of all commercial banks in Kenya. A similar study should also be done whereby the data collection relies on primary data i.e. in-depth questionnaires and interview guide so as to complement this study.

The study also recommends that a similar study to be done on other firms in other sectors such as the telecommunication and the banks to allow for generalization of the effect of mergers and acquisitions on performance. This is because different sectors have different strategic and financial policies.

The study also recommends that further studies should be done on the effect of bancassurance on the financial performance of insurance companies. This will enable one to get the effect of bancassurance from an insurance point of view.
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Appendix I: Commercial Banks Offering Bancassurance Services

1. Equity Bank
2. Chase Bank
3. CFC Stannic Bank
4. Diamond Trust Bank
5. Kenya Commercial Bank
7. Commercial Bank of Africa
9. Cooperative Bank of Kenya