

**DIVERSIFICATION AS A STRATEGIC ORIENTATION BY
INSURANCE COMPANIES IN KENYA**

BY

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**A RESEARCH PROJECT SUBMITTED TO THE SCHOOL OF
BUSINESS IN PARTIAL FULFILMENT OF THE REQUIREMENTS
FOR THE AWARD A MASTER OF BUSINESS ADMINISTRATION
DEGREE OF THE UNIVERSITY OF NAIROBI.**

OCTOBER, 2013

DECLARATION

This research project report is my original work and has not been presented for the award of a degree in any other university.

Signed Date.....

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This research project report has been submitted for examination with my approval as university supervisor.

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ACKNOWLEDGEMENTS

This research project was made possible through input of several people.

My special thanks and appreciation go to my supervisor and moderator for their sincere and honest encouragement and professional guidance while doing this study. My special thanks also go to the respondents who took time to give responses to the questionnaire especially my fellow colleagues in the industry.

Further, I wish to acknowledge my indebtedness to all my lecturers, administrative and support staff of the MBA program of the school of business that made my pursuit for knowledge comfortable and fruitful at the university.

DEDICATION

This research project is dedicated to my wife Pamela Aoko Okemwa and my children Naomi, Victor, Patience and Emmanuel for their understanding and encouragement during the period I was away from home undertaking this research. Their combined support and constant prayers gave me the much needed energy and encouragement to continue working very hard up to the completion of the course.

ABSTRACT

In today's business environment, products and services can be rendered obsolete within months and corporate market shares at risk almost on a daily basis, hence the reason why strategic management and diversification are topics of great interest in the insurance industry today. The insurance industry experiences various challenges in its operating environment especially in the developing countries like Kenya. There is widespread customer dissatisfaction in the insurance industry, stemming from insurers' failure to provide diversified product and service portfolio to satisfy customers' ever changing needs and wants. In an effort to cope with such challenges the insurance companies use different diversification strategies to not only remain profitable but also become stable financially. This study utilized a descriptive survey design on the diversification strategies which insurance companies in Kenya use to remain profitable and stable. This study, therefore, sought to find out diversification strategies which the insurance companies use to attain their targets. Data was collected from a sample of fifteen insurance companies selected from a total of forty six firms operating in Kenya. The researcher used convenient random sampling technique to obtain the required data. The researcher collected data using a structured questionnaire which were sent using either electronic mail or hand delivered to the respondents who filled the questionnaire for later collection. The collected data was analyzed using descriptive statistics which included the arithmetic mean, median and mode and this was used to answer the research questions. The study found out that concentration on the core business of selling insurance is the most popular diversification strategy among insurance companies operating in Kenya. However some other insurance companies have done unrelated diversification in other areas like real estate management, property management, warehousing, agriculture, banking, stock market, and other areas of the economy. It is recommended that insurance companies should concentrate on their core activities as they diversify into other areas to supplement their income

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CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

In today's business environment, products and services can be obsolete within months and corporate market shares at risk almost on a daily basis, hence the reason why strategic management is a very hot topic in business today. The strategies that are used have critical influence on strategic business outcomes. Currently, management practices, in terms of the convergence of information flows, products and service flows, logistics, and payment flows, are transforming the ways that companies produce goods, market them and provide services and hence create increasing value for customers (Gekonge, 2006).

The insurance industry experiences various challenges in its operating environment especially in developing countries like Kenya. Key among them is poor public perception of insurance. There is widespread customer dissatisfaction stemming from insurers' failure to satisfy customers' needs through prompt claims settlement. A number of insurance companies have gone under receivership putting their customers in great danger of unprotected assets and at the mercy of courts. The Association of Kenya Insurers (AKI) in conjunction with other stakeholders continues to engage the Government of Kenya in order to come up with lasting solutions to these challenges. It is commendable to note that the government, on its part, has initiated a comprehensive review of the Insurance Act. The process is expected to identify any weaknesses, gaps or inconsistencies in the existing law that may have hampered the growth and

development of the insurance industry. The new Insurance Act is expected to accelerate the growth and development of the insurance sector tremendously (AKI, 2008).

1.1.1 Concept of Strategy

Scholes (2008) conceptualizes strategy as the direction and scope of the firm over the long term meant to deliver a competitive advantage for the organization in an environment which is ever changing. Strategy is considered to be effective if it has the capability to transform firm's core competencies and resources so as to not only meet but surpass the goals and objectives of the firm. An effective strategy therefore forms the basis of a strong firm culture whose core focus is on value adding mandates in its mission and vision. Accordingly therefore, competitive strategy must create a fit between the internal resource capabilities of the firm and the external environmental changes facing the firm. A disjoint between the capabilities and the environment is a recipe for firm Strategy therefore as the overall goal of creating a competitive position in the firms overall market failure (Aosa, 1992).

Strategy is also considered to be a ploy, a plan, a position or a perspective whose core intension is to create competitiveness for the firm (Mintzberg, 1994). It is a pattern which amalgamates organization goals, objectives and policies underlines them with the firm's resource capabilities to tap on environmental opportunities and proactively or otherwise deal with the threats occasioned by environmental turbulence (Mintzberg, & Quinn, 1991). Overall strategy creates roadmap of the firm which precisely gives a definition of the exact business in which the form exists to undertake, the aspirations of the firm and

the direction the firm intends to take with core intension of stakeholder interest maximizations.

Competitive strategy is aimed at creating firm profitability and a competitive position of the firm which places the firm a head of its competitors through superior performance. This is done through effective moderation of the challenges in the external environment as well as offering of product of greater quality to customers (Ansoff & McDonnell , 1984). The concept of strategy if properly applied can only achieve organization success by constantly changing in line with environmental changes. It is for the reason that strategic managers in the contemporary world of business must constantly shift their strategy gears from intended strategy to emergent strategy or a combination of the two depending on environmental changeability

1.1.2 Diversification Strategy

A common feature of the industrial landscape of most emerging economies today is the existence of diversified business groups. Many contemporary studies of business groups (Chang and Choi, 1988; Khanna and Palepu, 1998, 2000; Khanna and Rivkin, 2001; Kim et al., 2004) have established that diversification is beneficial in emerging markets, unlike in developed economies where diversified companies are valued at a discount. Khanna and Palepu (1998, 2000) have also examined the extent of diversification and firm value, arguing that beyond a threshold diversification is beneficial. The predominant rationale for the existence of groups that researchers explore in literature relates to transaction cost economics and weaknesses in market institutions. The resource perspective which is our focus is relatively underutilized perspective by researchers, and we believe has a potential

to enhance our understanding of group existence and performance link. Guillen (2000) argues that pooling and distribution of heterogeneous resources through related and unrelated diversification is an important role of business groups through which they add value to affiliated firms. But there are no studies that examine the performance impact of either of the two diversification strategies (related/unrelated) in business groups in emerging markets. Our work seeks to address this gap in literature by examining the direction of diversification and its impact on group's value. Hitt et al. (2004).

The resource-based view seems to suggest that firms diversify into related industries and related diversification leads to superior rents (Montgomery and Wernerfelt, 1988; Rumelt, 1974). The firm resources include the factors of production, services created from the factors of production and the specialized competencies it has created over time (Penrose, 1959). According to the resource-based view, firms diversify in response to the excess capacity in the resources they possess (Penrose, 1959).

Therefore, as long as the firm can find profitable ways of exploiting its unutilized resources, it has incentive to expand (Montgomery and Wernerfelt, 1988). The unutilized resources of the firm offer the potential to exploit scale and scope benefits. The exploitation of economies of scale is available through the exploitation of firm-specific resources into related industries. Nayyar (1993) contends that benefits of positive reputation and economies of scope are exploitable from related diversification, but are unavailable from unrelated diversification. These conditions of resources strongly point to diversification that is related and therefore the RBV suggests a positive relation between firm performance and related diversification. Rumelt (1974) conjectures related

diversification to be a better strategy in comparison to unrelated diversification. Hence, extending the arguments proposed in the resource-based theory to diversified business groups in emerging markets we conjecture that in addition to the positive effects of group affiliation on firm value (that transaction cost economics predicts), related diversification is a rewarding strategy for business groups.

1.1.3 Insurance Industry in Kenya

The concept of insurance and particularly the social insurance programme dealing with socio-economic problems has been around Africa for a long time (Kenyatta, 1962). Members of a community pooled together resources to create a social insurance fund. The premiums ranged from material to moral support or other payments in kind. From the fund, drawings were made out to support the few unfortunate members exposed to perils (Azevedo, 1993). However, the history of the development of commercial insurance in Kenya is closely related to the historical emancipation of Kenya as a nation (Throup, 1988).

With the conquest of Kenya as a British colony complete, settlers initiated various economic activities, particularly farming and extraction of agricultural products (Huxley, 1990). These substantial investments needed some form of protection against various risk exposures. British insurers saw an opportunity in this, and established agency offices to service the colony's insurance needs. Prosperity in the colony soon justified expansion of these agencies to branch networks with more autonomy, and expertise to service the growing insurance needs. By independence in 1963, most branches had been transformed to fully-fledged insurance companies (Maxon, 1993).

At the end of 2011 there were 46 licensed insurance companies. 22 companies wrote non-life Insurance business only, 9 wrote life insurance business only while 14 were composite (both life and non-life). There were 163 licensed insurance brokers, 23 medical insurance providers (MIPs) and 4223 insurance agents. Other licensed players included 120 investigators, 80 motor assessors, and 21 loss adjusters, 2 claims settling agents, 10 risk managers and 26 insurance surveyors.

The gross written premium by the insurance industry in Kenya was Kshs 79.10 billion in the financial year 2011. The gross written premium from Non-Life insurance was Kshs 52.35 billion while that from life insurance business was Kshs 26.71 billion. Industry earnings from investment and other income increased by 58.3% from Kshs. 15.10 billion in 2009 to Kshs. 23.93 billion in 2011. The combined industry profit after taxation increased by 79.5% to Kshs. 7.70 billion in 2011 compared to Kshs. 4.29 billion in 2010. The overall underwriting profit posted under non-life insurance was Kshs. 1.27 billion compared to Kshs. 414 million in 2010

Insurance functions as a mechanism to diversify risks, similar to the role of mutual funds in diversifying investment risks. In fact, because insurers accumulate substantial funds in conducting their business, they also diversify investment risks for their stakeholders by investing in diversified portfolios. Insurance along with banking, investment and savings form a very significant part of the immensely important financial services sector in any economy. Although these are really separate disciplines there is some overlap. Insurance allows both businesses and individuals to minimize the impact of financial loss, resulting

from the occurrence of future events and enables policyholders to organize a household budget or plan business activities with greater security.

1.2 Research Problem

Diversification has always been an important issue in strategic management. Many researches discussed the relationship between diversification strategy and firm performance. The issues include firm performance with degree of diversification (Geringer, Tallman & Olsen, 2000), product diversification (Mayer & Whittington, 2003; Qian 1997), “geographic (or international) diversification (Delios & Beamish, 1999; Thomas, 2006; Qian and Li, 2002).

The future of the insurance industry appears to be very bright given the huge untapped market (with insurance penetration at a mere 3.63%), increasing usage of ICT, utilization of alternative distribution channels, research and product development. The government recognizes the important role played by the insurance sector in the growth of the Economy and it has identified the industry as a major player in the financial sector in the achievement of Vision 2030 (AKI, 2008)

The Association of Kenya Insurers continues to request government through the Insurance Regulatory Authority to consider making insurance legislation that will uplift financial intermediaries in the country. Government should also bring its assets to the insurance market rather than carrying the random cost and frequency of risk on its balance sheet. The prospective provision of employee life and medical insurance benefits to civil servants would provide a benchmark for all employers in the country, bring to the

fore the uplift of the insurance mechanism and exit the culture of fund-raising from its desperate features to a purely compassionate expression.

The insurance industry has always invested heavily in the different sectors of the economy. The investment income has also increased tremendously to a high of Kshs. 23.93 billion in the financial year 2010. The role of the insurance industry is to provide economic protection from identified risks. The activities of insurance companies include underwriting insurance policies (including determining the acceptability of risks, the coverage terms, and the premium), billing and collecting premiums, and claims made under policies.

The insurance industry service providers have diversified their operations into related and unrelated activities. Several insurance companies have diversified their operations outside our borders into other markets including Uganda, Tanzania, Southern Sudan, Rwanda and others regions. Several insurance companies own several buildings within the city centre for commercial purposes, control the Nairobi stock exchange, own several residential buildings for commercial gains. Others have also invested heavily unrelated areas that include securities, properties, mortgages and loans.

Several studies have been done on in the field of diversification strategies in different industries, sectors and organizations in Kenya. Lole (2009) conducted a study on diversification strategies in the banking industry in Kenya. He found that the banking industry in Kenya use mainly three types of strategies namely horizontal diversification, vertical diversification and geographical diversification strategies to compete effectively

in the market. The most used strategy was the horizontal diversification followed by geographical diversification. Mwangi (2010) conducted a study on implementation of the diversification strategy at the Standard group (K) Ltd. He found that the Standard group adopts the diversification strategies to maximize and compete effectively in the media market.

Musila (2009) did a study on the application of the diversification strategy at the Anglican church of Kenya. She found that the church uses the related diversification strategies to sustain its core mission, generate sufficient profits for supporting the church activities and for future growth. Others studies include; Mwindi (2003) who conducted a study on an analysis of the application of unrelated diversification strategy by major oil companies in Kenya, Mwau (2005) did a study on related diversification in the East Africa Building Society Ltd, Njoroge (2006) did a case study on Kenol/Kobil on building a competitive advantage through diversification, Wakwoma (2007) conducted a survey on product diversification strategies adopted by firms in the banking industry in Kenya while Munene (2008) did a study on diversification strategies of Christian community services of Mount Kenya East region.

To the best knowledge of this researcher, no known studies have been done on the diversification as a strategic orientation by insurance companies in Kenya. This study therefore sought to answer the question; how has diversification as a strategic orientation been utilized by insurance companies in Kenya?

1.3 Research Objectives

The research objectives of this study were:-

- (i) To determine the extent of diversification as a strategic orientation by insurance companies in Kenya
- (ii) To determine the challenges involved in such strategic orientation.

1.4 Value of the Study

It is hoped that the study findings will help scholars understand diversification as an important tool of strategic management. The findings of this study will make valuable contributions to the academicians who may find useful research gaps that may stimulate interest in future research in the area of diversification. This will form the basis of literature review for future researchers.

In terms of policy formulation and implementation, the study findings will help insurance companies not only adapt but also understand the areas of diversification to increase their stability and profitability. Insurance managers will also find the study findings of great significance in the creation of competitive edge through the concept of diversification.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

The insurance industry operates in a very volatile environment causing various challenges especially in the developing countries like Kenya. Key among such challenges is the poor public perception of insurance companies which is mainly caused by delayed claims settlement and insurers' failure to satisfy customers' needs. As a result the insurance industry is diversifying its businesses in order to remain competitive and gain advantage in the market. This chapter therefore discusses diversification as a strategy, the different diversification strategies employed and the benefits of such diversification strategies.

Typically, large firms with complex organizations and agency problems are diversified across more than one country and/or industry. It is largely documented that diversified firms are generally larger, that they have more complex organizational structures, have less transparent operations and that their analysis poses difficulties to investors and analysts alike (Chang and Yu, 2004; Kim and Pantzalis, 2003; Liu and Qi, 2007; Rodri'guez-Pe' rez and Van Hemmen, 2010). In addition, they are likely to exhibit agency conflicts and informational asymmetry problems. (Dye, 1988; Trueman and Titman, 1988). It is argued that managers may seek to diversify to increase their compensation (Jensen and Murphy, 1990), power and prestige (Jensen, 1986), secure their position within the firm through specific investments (Shleifer and Vishny, 1990a and b) and Reduce the risk of their personal investment by reducing firm risk (Amihud and Lev, 1981).

Kenya is categorized as an emerging market. The assumptions of emerging markets are that the capital market structure is imperfect and underdeveloped. Khanna and Palepu (1997) suggest that these imperfections exist in the labor, capital and product markets as well. Transaction cost economics predicts that internal capital markets would be an efficient alternative under these conditions. Therefore, firms will have incentive to diversify. The transaction cost economics theory also predicts that diversified firms will outperform focused firms in imperfect markets.

Because transaction cost economics predicts favorable effects of diversifying as a strategy, it follows that firms that have a dominant diversified structure would be valued more by the market. Diversification strategy is typically executed through the group structure although many focused business entities also emulate the group structure. Khanna and Palepu (1997, 1999b, 2000) and Perotti and Gelfer (2001) show that industrial groups commonly exist in emerging markets. Therefore, a positive impact of group affiliation (and therefore diversification) on firm value is expected and is a well researched proposition by authors examining business groups in emerging markets (Khanna and Palepu, 1998, 2000; Lins and Servaes, 2002).

2.2 Concept of Diversification Strategy

In reviewing the evidence on diversification, Howe has concluded that as a strategy it “has not lived up to expectations”. One recent study of strategic response to recession by Whittington, for example, concluded that diversification had little positive impact on performance. Indeed, Kastens has voiced a widely held view that diversification is

basically a negative strategy involving companies running away from fundamental problems. The difficulties involved with diversification have been well aired in the literature. Diversification is often viewed as a panic measure which suffers from a lack of strategic planning. Moreover, management skills may not be easily transferable to a new area of business. It is generally agreed that to attempt simultaneously to enter new markets and develop new products is a risky strategy which should be avoided if at all possible. The degree of relatedness of the new area of business with a company's existing business has also been thought to be of some importance to the likely success of diversification. A recent study by Very, for example, argues that the key to successful diversification is building on the core competences of a business and that superior performance through diversification is primarily based on relatedness.

Warnings concerning the potential pitfalls of diversification have been echoed by some studies in some industries. The problems which were identified included a lack of ability to create new products, control costs or market activities adequately. A survey in *Management Today* also documented a series of weaknesses in the strategies of many leading companies. Some of the problems at British Aerospace have also been judged to be related to a badly timed and over-ambitious programme of diversification.

2.3 Diversification as a Strategic Orientation

There have been several arguments stated in the literature to explain why firms diversify. Rooted in industrial economics, the market power view emphasizes the risk of anti-competitive effects of diversification (Montgomery, 1994). Thus, conglomerate companies may exercise market power (Edwards, 1955; Hill, 1985) through e.g. cross-

subsidization and predatory pricing activities, the exploitation of cost opportunities due to synergy effects, reciprocity in buying and selling among large diversified firms which creates or raises entry barriers to smaller competitors (Palepu, 1985). Applying the ideas of industrial economics to the individual enterprise, Porter pointed out that industry characteristics might be exploited strategically to increase a firm's performance (Porter, 1980), thereby arguing that diversification is positively related with performance if a firm is able to generate opportunities in one business or reduce risk in another by diversifying its activities (Caves, Porter & Spence, 1980). Derived from portfolio theory and related to the imperfections of capital markets, some studies indeed found evidence for diversification as a means of balancing investment risk (i.e. Markham, 1973). Under perfect capital market conditions, however, diversification is said to provide no benefits to shareholders since they can diversify their portfolios on their own (Amihud & Lev, 1981).

According to the work of Penrose (1959) and presuming that firms often possess pools of not fully exploited or unused resource capacities (Mahoney & Pandian, 1992), the resource view focuses on corporate diversification as a strategic growth option (Ramanujam & Varadarajan, 1989). A company has several opportunities to take advantage of its excess capacities (Teece, 1982): They can be reinvested in the firm's traditional business or be sold to other firms in other markets. Unused resource which can be translated into free cash flow could be returned to stockholders through higher dividends. Firms with excess capacity in resources could also diversify into other markets, either through acquisition or new market entry. Assuming that firms choose a

strategy in order to generate rents based upon their resource capabilities (Mahoney & Pandian, 1992), rent-seeking firms thus diversify as long as diversification provides a way of more profitably employing its underused resources (Teece, 1982; Montgomery & Wernerfelt, 1988).

The agency theory considers corporate diversification as a result from the separation of ownership and control which gives managers the opportunity to pursue their own objectives at the expense of shareholders (Jensen & Meckling, 1976). Excessive expansion through diversification might thus occur because of different reasons: In order to increase the firm's demands for their individual skills and knowledge (Shleifer & Vishny, 1989) or to diversify the managers' own employment risk (Amihud & Lev, 1981). As the firm's growth often augments not only their compensation, but also the resources under managers' control and therewith their power, managers have incentives to cause their firms growing beyond the optimal size (Jensen, 1986).

Dynamic entrepreneurial growth processes may provide an explanation for the formation of diversified firms. Among others, Rosa (1998) and Iacobucci & Rosa (2005) analyzed growth processes of entrepreneurial firms which they defined by being owned and controlled by the same entrepreneur or entrepreneurial team. The unity of ownership and control eliminates and at the same time broadens some of the main arguments traditionally stated in the diversification literature, especially those associated with agency costs arising from the separation of ownership and control. Other arguments may be referred to in order to explain diversification decisions in an entrepreneurial firm: From a portfolio perspective, the entrepreneur might diversify in unrelated business in

order to reduce specific risk, if his or her personal wealth is concentrated in entrepreneurial activities he or she controls directly. Very often the entrepreneurial growth process is much less determined by planning activities than in large, managerial firms. In an entrepreneurial firm, the decision to pursue a diversified activity is often rather a 'product of serendipity and opportunism' (Iacobucci & Rosa, 2005, p. 69).

Jaffe & Lane (2004) stated that business need well-established governance structures and processes to be able to ensure continuing wealth creation for future generations and to create an effective dynasty over generations. They observed that corporate diversification appears to be a prevalent strategy especially of multigenerational family firms which are characterized by multiple family branches. Even though, following Jaffe & Lane (2004), there are some issues detaining diversification decisions in family firms: Due to the personal relationships within the owner-family, it might be difficult for a family member to take responsibility for a failed investment.

Furthermore, businesses very often invest in large asset classes which ties up resources necessary to diversify and enter new markets. Those new markets may lie beyond their knowledge and expertise, again restraining diversification decisions. Besides, family firms often exhibit a strong emotional attachment to the firm's founder's business which might make it difficult to diversify. Jaffe & Lane (2004) emphasize that family dynasties need a sound and agreed to investment philosophy to multiply their portfolio successfully. This study as well does not deliver concrete information on the underlying definition of a family firm.

2.3.1 Concentric Diversification Strategy

Concentric diversification occurs when a firm adds related products or markets. The goal of such diversification is to achieve strategic fit. Strategic fit allows an organization to achieve synergy. In essence, synergy is the ability of two or more parts of an organization to achieve greater total effectiveness together than would be experienced if the efforts of the independent parts were summed. Synergy may be achieved by combining firms with complementary marketing, financial, operating, or management efforts. Breweries have been able to achieve marketing synergy through national advertising and distribution. By combining a number of regional breweries into a national network, beer producers have been able to produce and sell more beer than had independent regional breweries. The technology used in the industry remains the same, while the marketing plan changes to a significant extent. Hence this strategy requires technological similarities between the two business ventures (Ramirez, 1995).

2.3.2 Conglomerate Diversification Strategy

Conglomerate diversification occurs when a firm diversifies into areas that are unrelated to its current line of business. Synergy may result through the application of management expertise or financial resources, but the primary purpose of conglomerate diversification is improved profitability of the acquiring firm. Little, if any, concern is given to achieving marketing or production synergy with conglomerate diversification.

One of the most common reasons for pursuing a conglomerate growth strategy is that opportunities in a firm's current line of business are limited. Finding an attractive investment opportunity requires the firm to consider alternatives in other types of

business. Firms may also pursue a conglomerate diversification strategy as a means of increasing the firm's growth rate. Growth in sales may make the company more attractive to investors. Growth may also increase the power and prestige of the firm's executives. Conglomerate growth may be effective if the new area has growth opportunities greater than those available in the existing line of business. Probably the biggest disadvantage of a conglomerate diversification strategy is the increase in administrative problems associated with operating unrelated businesses. Managers from different divisions may have different backgrounds and may be unable to work together effectively. Competition between strategic business units for resources may entail shifting resources away from one division to another. Such a move may create rivalry and administrative problems between the units (Amit, and Livnat, 1988)

2.4 Related and unrelated diversification Strategy

Geographic diversification: Pro-conglomeration arguments suggest that geographically diversified firms are likely to have less volatile profits due to coinsurance effects. As a result of their lower risk, geographically diversified insurers should be able to charge higher prices than geographically focused insurers, all else equal. These arguments suggest a positive relation between the degree of geographic diversification and risk-adjusted performance. By contrast, pro-focus arguments suggest that geographically focused insurers are able to avoid costly monitoring that is required when operating across different states (Winton (1999)) and achieve efficiencies arising out of market specialization.

Industry concentration: The structure-conduct-performance paradigm suggests a positive relation between industry concentration and prices. Chidambaran, Pugel and Saunders (1997) find a positive relation between prices and market concentration in P/L insurance lines. We therefore follow Montgomery (1985) in controlling for the concentration of industries in which a firm participates. Montgomery argues that, *ceteris paribus*, firms operating in more concentrated industries are likely to benefit from higher prices and higher profits.

2.4.1 Unrelated Diversification

The arguments presented so far explain the decision to exploit resources that are valuable across industries. A central prediction of these literatures is that related diversification should outperform unrelated or conglomerate diversification. And yet, the US conglomerates that arose in the 1960s did not, despite the restructuring of the 1980s, disappear from the corporate scene. Rumelt (1982) reports that the percentage of Fortune 500 firms classified as “single business” fell from 42.0 in 1949 to 22.8 in 1959, and again to 14.4 in 1974, while the percentage of “unrelated business” firms rose from 4.1 in 1949, to 7.3 in 1959, to 20.7 by 1974. Servaes (1996), using SIC codes to measure diversification, finds a similar pattern throughout this period. Among firms making acquisitions, the trend is even stronger: pure conglomerate or unrelated-business mergers, as defined by the FTC, jumped from 3.2 percent of all mergers in 1948–1953 to 15.9 percent in 1956–1963, to 33.2 percent in 1963–1972, and then to 49.2 percent in 1973–1977 (Federal Trade Commission, 1981).

Moreover, despite evidence of de-diversification or refocus during the 1980s (Lichtenberg, 1992; Liebeskind & Opler, 1995; Comment & Jarrell, 1995), major US corporations continue to be diversified. Montgomery (1994) reports that for each of the years 1985, 1989, and 1992, over two-thirds of the Fortune 500 companies were active in at least five distinct lines of business (defined by four-digit SIC codes). As she reminds us, “While the popular press and some researchers have highlighted recent divestiture activity among [the largest U.S.] firms, claiming a ‘return to the core,’ some changes at the margin must not obscure the fact that these firms remain remarkably diversified” (Montgomery, 1994, p. 163). Baldwin, Beckstead, Gellatly, and Peters (2000) estimate that 71 percent of corporate diversification among Canadian companies occurs across two-digit SIC codes. In the developing world, conglomerates are even more important, accounting for a large share of economic activities in countries like India and Korea (Khanna & Palepu, 1999, 2000). On the whole, the evidence suggests that appropriately organized conglomerates can be efficient (Klein, 2001; Stein, 2003).

Arguments about resource substitutability and complementarity do not apply to unrelated diversification. Can unrelated diversification be efficient, or is it simply a manifestation of agency costs, a form of empire building, or a response to antitrust restrictions on horizontal expansion? Williamson (1975, pp. 155–175) offers one efficiency explanation for the multi-industry firm, an explanation that focuses on intra-firm capital allocation. In his theory, the diversified firm is best understood as an alternative resource-allocation mechanism. Capital markets act to allocate resources between single-product firms. In the diversified, multidivisional firm, by contrast, resources are allocated via an internal capital market: funds are distributed among profit-center divisions by the central

headquarters of the firm (HQ). This miniature capital market replicates the allocate and disciplinary roles of the financial markets, ideally shifting resources toward more profitable activities.

According to the internal-capital-markets hypothesis, diversified institutions arise when imperfections in the external capital market permit internal management to allocate and manage funds more efficiently than the external capital market. These efficiencies may come from several sources. First, HQ typically has access to information unavailable to external parties, which it extracts through its own internal auditing and reporting procedures (Williamson, 1975). Second, managers inside the firm may also be more willing to reveal information to HQ than to outsiders, since revealing the same information to the capital market would also reveal it to rivals, potentially hurting the firm's competitive position. Third, HQ can intervene selectively, making marginal changes to divisional operating procedures, whereas the external market can discipline a division only by raising or lowering the share price of the entire firm. Fourth, HQ has residual rights of control that providers of outside finance do not have, making it easier to redeploy the assets of poorly performing divisions (Gertner, Scharfstein, & Stein, 1994). More generally, these control rights allow HQ to add value by engaging in "winner picking" among competing projects when credit to the firm as a whole is constrained (Stein, 1997). Fifth, the internal capital market may react more "rationally" to new information: those who dispense the funds need only take into account their own expectations about the returns to a particular investment, and not their expectations about other investors' expectations. Hence there would be no speculative bubbles or waves.

If unrelated diversification is primarily a response to internal-capital- market advantages, rather than a manifestation of agency problems, then unrelated diversifiers should perform better than specialized firms, particularly when external capital markets are weak. And yet, the evidence on the value of unrelated diversification is mixed. Consider, for example, the “diversification-discount” literature in empirical corporate finance. Early studies by Lang and Stulz (1994), Berger and Ofek (1995), Servaes (1996), and Rajan, Servaes, and Zingales (2000) found that diversified firms were valued at a discount relative to more specialized firms in the 1980s and early 1990s.

2.5 Benefits of Diversification

There are several advantages for firms to diversify, whether industrial diversification or geographical diversification. Diversification can be driven by a number of perceived potential benefits associated with more efficient allocation of resources through internal capital markets, greater market power, utilization of excess resources or assets, reduced performance variability by the portfolio of imperfectly correlated set of businesses (Chakrabarti, Singh, & Mahmood, 2007) The first advantage is internal market efficiencies. Gains from diversification often relate to market failure (Ghemawat & Khanna, 1998). When the firm focuses on a single industry, it would be difficult for the firm to leverage its resources and capabilities efficiently to other products/industries/countries (Palich, Cardinal & Miller, 2000). By diversifying, firms create internal markets that may be more effective than inefficient external markets (Ghemawat & Khanna, 1998). Internalization of markets offers some benefits to firms such as economies of scale, scope and learning (Caves, 1982) and sharing core competencies among different business segments and geographic markets (Hamel, 1991).

The diversified firm has more flexibility and opportunity in capital formation because it can alternatively choose external market or internally generated resources (Lang & Stulz, 1994). When a diversified firm wants to grow, it can not only attract external capital for expansion, but transfer the internal resources or capitals from its portfolio (Palich, Cardinal & Miller, 2000). Diversification makes it possible for the firm to generate efficiencies from internal market that are unavailable for the single-business firm.

The next is market power advantage. Diversified firms employ several mechanisms and opportunities to create and exploit market power advantages which might be unavailable to focused firms (Caves, 1981). One important benefit from market power advantage is predatory pricing which is generally defined as sustained price cutting designed to drive the existing competitor out of the markets or discourage potential rivals from future entry. Diversification makes it possible for firms to blunt the efforts of competitors via predatory pricing. While predatory pricing causes losses, the losses usually are offset with gains from future profits. In addition, diversified firm can cross subsidize the losses with the revenues from other product line to support another (Palich, Cardinal & Miller, 2000).

Beyond the advantage of market power and internal market efficiency, better allocation and maximized utility of the resources is another benefit of diversification. Due to superior access to information, diversified firm can optimize the allocation of the resources (Palich, Cardinal & Miller, 2000). For example, the management of the diversified firm can direct capital away from slow-growing, cash-generating, operations to businesses that are expanding rapidly and have greater commercial and profit potential

but need investment. Diversification may also permit a firm which has firm-specific resources that are difficult to be sold out due to transaction costs or other imperfections to exploit the resources that would be underutilized in other business (Markides, 1992). Focused firms do not have multiple businesses to enjoy scope economies. Diversified firms have the opportunities to exploit between-unit synergies or the portfolio effects that are not available for focused firms (Lubatkin & Chatterjee, 1994). Single-business firms suffer from limited economies of scope and other disadvantages.

From the viewpoint of risk spreading, diversified firm would be better than focused firm because of its portfolio of imperfectly correlated set of businesses. According to Lubatkin and Chatterjee (1994), focused firms bear greater risks since they did not spread the risks by diversifying into several less perfectly correlated businesses. One of the reasons for conflicting results in previous studies about the relationship between group-level diversification and performance may be that few studies explored the impact of different diversification forms on the firm's performance. Here, we divided group-level diversification into three different forms: related diversification, unrelated diversification and geographic diversification.

2.5.1 Related Diversification and Performance

One advantage of diversification is the economies of scope. According to Nayyar (1992), related diversifiers involved in several industries are able to tap a common pool of corporate resources. Since related diversifiers are related in certain areas, the business group is capable of sharing resources or competences by bundling products, enjoying the windfall from a positive brand reputation, and the like (Barney, 1997). By sophisticated designing portfolio of mutually reinforcing businesses, the operational synergies are

generated by related diversifiers (Palich, Cardinal & Miller, 2000). As a result, related diversification may have superior advantage derived from economies of scope (Markides and Williamson, 1994). By the efforts as ‘asset amortization’ referred by Markides and Williamson (1994), a diversified firm is able to distribute the cost of an asset which is already capitalized by spreading its use across multiple operations.

In addition to the economies of scope, related diversifiers can convert underutilized assets by sharing resources and combining activities along the value chain. Just as the advantage of maximizing the utility of assets, related diversification helps to utilize the intangible assets and knowledge by spreading them across other operations such as intra-firm product/process technology diffusion. Beyond the advantages that we mentioned above, related firms may also benefit from learning curve efficiencies and restricted access to factors of production that are necessary for operating in a specific industry (Barney, 1997).

All of these advantages may contribute to a better performance for the related diversifiers. In addition, based on financial performance, Doukas (2003) found that related diversification is value-increasing for firms. When a firm engages in core-related investment transactions, it achieves higher gains and significant positive abnormal returns and profit margin gains. One important reason for related diversified business groups is that those related businesses may employ common or complementary resources such as technology, plants, brand names or distribution systems (Ghemawat and Khanna, 1998). Once these resources feature scale or scope of economies which cannot be effectively exploited through market transactions, it may be beneficial to business group to set up several different but related business or firms to make best use of these resources.

As a result, a more related-diversified business group may perform better than less related-diversified one because of the better utility of scale or scope of economies. Considering the features of business groups, namely, more efficient internal markets than external markets, as well as the network that is constituted by legally independent firms but cooperates with each other, business groups are more likely to achieve the benefit of related diversification. Through the internal markets between legally independent firms, business groups tend to achieve market efficiency and reduce organizational inertia. On the other hand, the legally independent firms belong to the same network which may reduce the transaction cost and opportunism. Specifically, business groups usually exist in emerging countries where the external institutional environments are not complete or stable. Under these imperfect contexts, business groups are more likely to attain the internal market efficiency compared to independent firms. By diversifying through creation of related firms, a business group typically attempts to exploit inefficient or absent markets and institutions in emerging economies (Chakrabarti, Singh & Mahmood, 2007).

2.5.2 Unrelated Diversification and Performance

One advantage of related diversification is the sharing of resources and competence among the divisions. While when it comes to unrelated diversification, due to the difficulty of sharing activities and transferring competences among different units, the costs of diversification seem to increase with unrelated diversification (Palich, Cardinal & Miller, 2000). Unrelated diversification may also interfere with the firm's core business operations and lead to significant operating inefficiencies resulting in negative

synergies among the different business segments. As a result, firms diversifying outside of their core businesses or competences may increase costs that might outweigh the potential benefit of unrelated diversification. Compared to related diversification, unrelated diversification seems unable to exploit the advantages of economies of scope and internal market efficiencies.

Unrelated diversification reduces the corporate focus of the firm and its existing operating efficiency (Doukas, 2003). In addition, Doukas (2003) found that multi-segment firms and single-segment firms both experience significant shareholder value losses when pursuing non-core-related international investments. The result implied that a business diversifying outside its core business, namely the unrelated diversification, would reduce its existing operating efficiencies and corporate cohesion due to lack of good fit and coordination with the core business of the firm. According to the explanation of Doukas (2003), the decrease in corporate focus is an important determinant of the unrelated diversification loss. Also, the misallocation of management time and other resource across business segmentation which are less likely to occur in related diversifying firm is one impediment to the performance of unrelated diversification.

It is realized that unrelated diversification hampers a corporation's performance because the lack of efficiency, coordination, cohesion and focus. While a business group contains several legally independent firms which seem not to have the problem of inefficiency and less corporate focus. With multiple legally independent firms managed by each firm's own CEO or top management team, a business group enjoys the advantage of spreading risk by unrelated diversification without the problem of losing its operating efficiencies and corporate cohesion. Although the affiliated firms belong to the network of business

group, they are independently operated and have their own operation plans and strategies which prevent them from the lack of focus of unrelated diversification.

One important feature of a business group is the core entity or administrative center offering common administrative or financial control (Leff, 1978), or managerial coordination among member firms (Khanna & Rivkin, 2001). The core entity has high autonomy and control over resources and information, which makes it possible for the core entity to influence other member firms in the business group (Yiu et al., 2007). Even that the member firms in a business group is unrelated, they are partially coordinated by the core entity. Thus, even the business group is unrelated diversified, it can still achieve the goal of coordination.

2.5.3 International Diversification and Performance

International diversification can be defined as a firm's expansion across different national borders. From Chandler (1962)'s point of view, international diversification represents a growth strategy that may be beneficial to a firm's performance. Similar to the advantage of related diversification, international diversification also offers some potential benefits to firms. Through internalizing markets, international diversification has the advantages of economies of scale, scope and learning as well as sharing core competences among several areas. International diversification offers market opportunities which provide firms with the opportunity to grow (Buhner, 1987).

Internationally diversified firms with strong competences developed at home have the chances to utilize the competences in international markets. When a firm is more involved in international market, it has more opportunities to exploit its tangible and

intangible resources which are expected to generate higher performance (Hymer,1976, Thomas, 2006). Since foreign direct investment into new national markets increases a firm's ability to utilize its intangible assets, foreign direct investment projects enhance the performance of the firm when they are directed in new countries where the firm does not have operations (Doukas, 2003).In addition, because foreign operations have greater growth opportunities than domestic operations, gains from foreign direct investment are larger when firms expand into new markets which implies that geographic diversification positively impacts on firm value (Doukas, 2003). Multinational firms have more opportunities to integrate their activities across borders by standardizing products, rationalizing production, and allocating their resources more efficiently and effectively (Kobrin,1991). By exploiting market imperfections, such as a less competitive environment, as well as cross-border transactions, multinational firms can gain additional competitive advantages.

If we perceive firm value as a firm's performance, several studies have concluded that international diversification increases the firm's performance. For example, Errunza and Senbet (1984) found support of a positive relationship between excess firm value and the firm's extent of international diversity. Morck and Yeung (1991) found a positive relationship between international diversification and firm value. For the shareholder value, Bodnar and Gebhardt (1999) found that shareholder value increases with global diversification. All of the studies above have shown that firm value is positively related to international diversification.

In a business group, the multiple ties among member firms enable them to take coordinated actions. Members of a business group may present a unified form to outside constituencies in different countries (Khanna & Rivkin, 2001). Similar to the concept of global strategic motivation (Kim & Hwang, 1992), we believe that business group with international diversification also have the same consideration. Global strategic motivation is defined as motivation which fulfills strategic aims set at the corporate level for the purpose of overall efficiency maximization (Kim & Hwang, 1992). In a business group where it is much easier to cooperate and coordinate than other independent firms, global strategic motivation may be more effectively achieve. In addition, an international diversified business group enjoys the benefit of multimarket power. Firms interacting in many different markets may be able to use those multiple interactions to support a less rivalries interaction (Ghemawat & Khanna, 1998).

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter sets out the research method that was followed in completing the study. It describes; design of the study, research instruments, collection methods and data analysis

3.2 Research Design

This research project adopted a census survey design. It covered 46 insurance firms in Kenya. It involved investigation of various diversification strategies adopted by insurance companies in Kenya and the basis of such diversification strategies. This research method was best suitable because of its wide area coverage of the entire insurance industry.

This research project adopted a descriptive survey research design to establish diversification as strategic orientation by insurance companies in Kenya. A descriptive survey design was necessary because the study was concerned with describing the characteristics of a particular group of firms thus the insurance companies. This was also necessary to obtain complete and accurate information from the insurance firm.

3.3 Population

This research project involved a census survey on the diversification strategies which insurance companies use to remain profitable and stable in Kenya. Such data could only be obtained from the members of management of the insurance companies involved. Therefore this project collected data from senior management staff only of 46 insurance companies. The required data on diversification was obtained from all the insurance

companies operating in Kenya. On average each insurance company has about five members of senior management staff. Since there are about forty six registered insurance companies in Kenya, the total population involved is about two hundred and thirty respondents.

3.4 Sample Design

The researcher used convenient random sampling technique to obtain the required data. This method of data collection has the advantage that it is cheaper and convenient to use. The researcher collected data from thirty percent of the total population of members of staff. This gave a sample of sixty six which is expected to be representative enough to provide the required data. The sample size included fifteen insurance companies with five members from each company bringing a total of seventy five.

The sample size is bigger than the sample taken by Gikanga (2008) who had a sample size of 10, Ngure (2001) who used a sample size of 40 and Arithi (2001) who had a sample size of 50. According to Ngure (2001), sample size can also be determined by the availability of resources which are very scarce especially in this study where the respondents are spread in different parts of the country.

3.5 Data Collection

Primary data of this study was collected using a structured questionnaire which was sent using either electronic mail or hand delivered to the respondents who filled the questionnaire for later collection. Some questionnaires were mailed especially to chief executive officers, to some of executive directors, while others were dropped and picked, and two were answered through telephone. These methods were used because they are

cheaper and convenient as most of the respondents were located around the city of Nairobi.

Also a face to face interview was conducted on a few selected respondents to get some clarifications and further explanations. The researcher also made a follow up using e-mail and telephone conversation to increase the number of returned questionnaires.

3.6 Data Analysis

All the returned questionnaires were thoroughly checked for any inconsistencies and errors which may have occurred during the process of data collection. Any such errors were corrected before analysis was done. The data was tabulated for analysis which included mainly descriptive statistics. Tables were used in summarizing the analyzed data and hence assist in answering the research questions. The descriptive statistics mainly include the arithmetic mean, median and mode and were used to give the picture or the general patterns of the diversification strategies which insurance companies use to remain profitable and stable in Kenya

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This study sought to establish the diversification strategies which insurance companies use to remain profitable and stable in Kenya. The study analyzed and interpreted responses to questions asked respondents on issues relating to the diversification strategies which insurance companies use. The responses were obtained from the different insurance companies operating in Kenya. Their responses were analyzed and discussed under the various headings in this chapter.

4.2 The Questionnaire

Data was collected using a questionnaire that asked different questions relating to the diversification strategies which insurance companies use to remain profitable and stable. The questions were put in a very simple language for ease of understanding and interpretation. Respondents were asked to state the extent of their agreement or disagreement with various statements relating to the diversification strategies.

4.3 Survey Response Rate

Out of a total number of 130 respondents targeted for this study, only 66 completed the survey instrument. This is because most of the respondents were most likely very busy with their daily operations and so did not see the need for answering the questions. The others saw no benefit of answering the questionnaire. Some of the respondents informed us that they were busy attending to their clients while others claimed they do not want to disclose their organisation strategies.

4.4 Results and Discussion

Respondents were asked different questions relating to the different diversification strategies that are commonly used by different organizations. The questions asked were related to concentration strategy, related and unrelated diversification strategies, backward and forward diversification strategies and intentional diversification strategies. Their respondents were recorded and discussed in the following paragraphs.

4.4.1 Concentric Diversification and Performance

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent, 4 means to a very small extent and 5 means not applicable or irrelevant) to which extent their company concentrates its core business (Concentric strategy). Their response was recorded as shown in table below.

Table I: Concentric Diversification and performance

Scale	No.	Percentage
1	34	51.5%
2	20	30.4%
3	6	9.1%
4	5	7.5%
5	1	1.5%
Total	66	100%
Mean average score $117/66 = 1.78$		

It is very clear from the data that 81.9% of insurance companies concentrate on their core business. This implies that insurance companies in Kenya use the concentric strategy to not only become profitable and financially stable.

Respondents also indicated that this strategy improves profitability/ stability of the company to the greatest extent. This agrees with the available literature that core business is the most important business of any organization. Hence the concentric strategy is mainly used by all insurance companies in Kenya.

4.4.2 Related Diversification and Performance

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent, 4 means to a very small extent and 5 means not applicable or irrelevant) the extent to which your company does business with other businesses in the same industry or acquires other businesses in the same industry. Their response was recorded as shown in table below.

Table II: Related diversification and performance

Scale	No.	Percentage
1	2	3.0%
2	4	6.0%
3	10	15.2%
4	15	22.8%
5	35	53.0%
Total	66	100%
Mean average score $275/66 = 4.2$		

Source: Research data

It is very clear from the above table below 10% of insurance companies do not concentrate in related diversification in the same industry. This means that the companies concentrate in related diversification to a very small extent.

The respondents indicated that the related diversification strategy contributes to profitability and stability of insurance companies to a very small extent. This is most probably because all the insurance companies operate in the same business environment and therefore may be exposed to the same operating conditions.

4.4.3 Backward Diversification and Performance

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent, 4 means to a very small extent and 5 means not applicable or irrelevant) the extent to which their company sources or assists in the procurement of its raw materials or services. Their response was recorded as shown in table below.

Table III: Backward diversification and performance

Scale	No.	Percentage
1	0	0.0%
2	2	3.0%
3	6	9.0%
4	15	22.8%
5	43	65.2%
Total	66	100%
Mean average score $297/66 = 4.5$		

Source: Research data

The data shows that the backward diversification strategy may not popular among most insurance companies operating in Kenya. Only 3% responded as having some sort of

backward diversification. This may be because it may not be expensive to procure raw materials for the companies. This strategy therefore contributes to profitability and stability of insurance companies to a very small extent.

4.4.4 Forward Diversification and Performance

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent, 4 means to a very small extent and 5 means not applicable or irrelevant) the extent to which their company distributes or assists in distributing its products or services. Their response was recorded as shown in table below

Table IV: Forward diversification and performance

Scale	No.	Percentage
1	2	3.0%
2	2	3.0%
3	6	9.0%
4	8	12.2%
5	48	72.8%
Total	66	100%
Mean average score $296/66 = 4.5$		

Source: Research data

The data shows that the forward diversification strategy may also not popular among the insurance companies operating in Kenya. Only 6% of the respondents acknowledge as

using the strategy in their companies. This may be because it may not be expensive to distribute final products to the various market outlets. This strategy therefore contributes to profitability to a very small extent.

4.4.5 Joint Ventures and Performance

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent , 4 means to a very small extent and 5 means not applicable or irrelevant) the extent to which their company involves itself in joint venture with other businesses in the same industry. Their response was recorded as shown in table below.

Table v: Joint Ventures and performance

Scale	No.	Percentage
1	12	18.2%
2	18	27.3%
3	21	31.8%
4	9	13.6%
5	6	9.1%
Total	66	100%
Mean average score $177/66 = 2.7$		

Source: Research data

The data shows 65.5% of insurance companies have joint ventures with others in the same industry. This is true as some insurance companies have merged while others have formed joint ventures to improve their profitability. This means that joint venture

improves profitability and financial stability of insurance companies to some reasonable extent.

4.4.6 Unrelated Diversification and Performance

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent, 4 means to a very small extent and 5 means not applicable or irrelevant) the extent to which their company create or acquire other businesses that distributes products/ services that are unrelated with its core business. Their response was recorded as shown in table below.

Table VI: Unrelated diversification and performance

Scale	No.	Percentage
1	3	4.5%
2	5	7.6%
3	45	68.2%
4	10	15.2%
5	3	4.5%
Total	66	100%
Mean average score $203/66 = 3.1$		

Source: Research data

The data shows that unrelated diversification strategy is used by more than two thirds (68%) of the insurance companies in Kenya. The respondents indicated that their companies are engaged in the construction industry, real estate management, banking,

brokerage business and in other areas of the economy. This shows that most insurance companies have used unrelated diversification to remain stable.

4.4.7 Important Strategies

Respondents were asked to indicate on a scale of 1-5 (where 1 means to very large extent, 2 means to a large extent, 3 means to a small extent, 4 means to a very small extent and 5 means not applicable or irrelevant) the extent to which those the diversification strategies, improve profitability/ stability of your employer. Their response was recorded as shown in table below.

Table VII: Important strategies

Scale	No.	Percentage
Concentric diversification	33	50.0%
Related diversification	5	7.5%
Backward diversification	0	0%
Forward diversification	0	0%
Joint Ventures	5	7.5%
Unrelated diversification	23	35.0%
Total	66	100%

The data shows that the concentric diversification strategy and the unrelated diversification strategies are most used diversification strategies by insurance companies in Kenya. According to the data the backward diversification strategy and the forward

diversification strategies are the most unpopular strategies and therefore may not be used by any of the companies.

From above analysis it is of importance to note that insurance companies in Kenya apply various diversification strategies. The main motive is to grow business as well as maximize profits. Due to various risk exposure insurance companies in addition to concentrating in their main areas of operation tend to invest in property development for rental income, set up subsidiary companies such as banks and asset management firms and expand into new areas both locally and internationally. The nature of strategy employed directly determines performance of the firm; diversified firms are more flexible in terms of capital generation, business growth and profitability. Firms are able to expand their markets and widely spread their risks. Large economies of scale are easily generated

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary of the research findings on diversification as a strategic orientation by insurance companies in Kenya, conclusions and recommendations are drawn there too. The chapter is hence structured into summary of findings, conclusions, recommendations and area for further research.

5.2 Summary of Findings

From the study, it was found that all the insurance companies concentrate in their core business of selling insurance. All of the companies under investigation were found to employ concentric strategy in their businesses. The findings indicated that 90% of insurance firms in Kenya concentrated on their core business of selling insurance products to generate increase revenues. This includes both life and general insurance business. However it was also found out that other insurance companies have diversified into unrelated businesses such as real estate. This mainly involves investment in building for both commercial and domestic purposes.

Majority of insurance companies have aimed at developing their own office block for personal use and rental income purposes. Such unrelated diversification has made the insurance companies to be more stable and spread their risks. Some companies have also invested in government securities both corporate and infrastructure levels as a source of additional revenue to not only be more profitable but also financially stable. It is there of

great importance for companies to implement various strategies in diversifying their operations.

5.3 Conclusion

The study concluded that concentration on the core business of selling insurance in the market is the most popular diversification strategy among insurance companies operating in Kenya. This is partly because the insurance law in Kenya does not allow insurance companies to do other businesses outside the insurance business. However investment of funds in other sectors of the economy thus diversification is allowed. Some insurance companies have therefore invested in other areas like real estate management, property management, warehousing, agriculture, banking, stock market, and other areas of the economy. This has made the diversified companies to be not only profitable but also financially stable.

The findings also indicate that the second most preferred diversification strategy is investment outside the core business in key areas such as the stock market and real estate management. At the same time insurance firms have undertaken regional and international market expansion to increase their customer base. Major insurance firms such as Jubilee have international investment both Tanzania and Uganda. Phoenix insurance company limited has also outside Kenya in countries such as Seychelles, Uganda and Burundi among others.

5.4 Recommendations

This study recommends that insurance companies operating in Kenya should concentrate on their core business thus concentric strategy and unrelated related diversification strategies not only to remain profitable but become financially stable. Those insurance companies that have diversified into unrelated businesses like in real estate, banking, information technology, Nairobi Stock exchange and other areas of the economy are among the most stable and profitable in the industry. Hence it is recommended that the other insurance companies should diversify into other areas so that they can not only improve their profits but also become very stable.

At the same time insurance companies should now operate in line with government policy and international standards whereby they are allowed to separate their operation and products into separate lines of business. For example instead of having composite company, life and general business lines are now required to be distinct entities. This is for the purposes of protecting the life fund.

5.5 Limitations of the Study

The numbers of questionnaires that were filled and were returned by respondents were generally less than the expected number and hence this may have had some impact on the data collected. The responses of some of the respondents may be personal and therefore may not represent the actual picture of the insurance companies operating in Kenya. The target respondents were very busy people who could not easily find time to complete the questions. This made the research take a lot of time in data collection. In some instances respondents misplaced questionnaires and had to be supplied again.

5.6 Areas for Further Study

Given the above limitations, researcher did not exhaustively cover the research objectives. The researcher therefore recommends more studies to be undertaken on the insurance industry. An areas such as a comparative study between related and concentric diversification strategies on the financial performance of insurance firms in Kenya will be of greater interest.

Also research can be done on the contribution of rapid diversification on poor performance of insurance companies in Kenya. In addition it will be necessary to undertake research on international diversification as a strategic orientation by insurance companies in Kenya. It is hoped that the findings of such studies would greatly contribute to general theory development and practice in the insurance industry in Kenya

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APPENDICES

APPENDIX I: QUESTIONNAIRE

PART I: BIO DATA OF RESPONDENTS

Dear respondent,

You are kindly requested to assist in filling this questionnaire on the diversification strategies used by insurance companies in Kenya to remain stable. Any information that you give will be treated in the strictest confidence and will not be used for any other purposes than for this research study.

Kindly spare a few minutes of your time to go through the questionnaire and answer the following questions as objectively as possible.

1. Name of the respondent -----
2. Title/ position of the respondent
3. Kindly indicate the category of your qualifications
 - i. Diploma
 - ii. Degree
 - iii. Post graduate
 - iv. other
4. Name of the employer.....
5. For how long have you worked for this company-----
6. Briefly explain your major duties-----
7. Kindly indicate the nature of your insurance business

PART II: DIVERSIFICATION STRATEGIES

In the following set of questions, the ranks, 1 mean a very large extent, 2 means large extent, 3 means small extent, 4 means a very small extent and 5 means not applicable or irrelevant).

8. Kindly indicate by tick the extent to which your company concentrates on the core business only?

1 2 3 4 5

9. Indicate to what extent this strategy improves profitability/ stability of the company?

1 2 3 4 5

10. Indicate to what extent your company does business with other businesses in the same industry or acquired other business in the same industry?

1 2 3 4 5

11. Indicate to what extent this strategy improves profitability/ stability your company?

1 2 3 4 5

12. Indicate to what extent your employer sources or assists in the procurement of its raw materials or services?

1 2 3 4 5

13. Indicate to what extent this strategy improves profitability/ stability of your company?

1 2 3 4 5

14. Indicate to what extent your employer distributes or assists in distributing its products or services?

1 2 3 4 5

15. To what extent does this strategy improve profitability/ stability of the company?

1 2 3 4 5

16. Indicate to what extent your company involves itself in joint venture with other businesses in the same industry?

1 2 3 4 5

17. Indicate to what extent this strategy improves profitability/ stability of the employer?

1 2 3 4 5

18. Indicate to what extent your employer acquires or distribute services which are related with the core business?

1 2 3 4 5

19. Indicate to what extent this improves profitability/ stability of the employer?

1 2 3 4 5

20. Indicate to what extent your company create or acquire another business that distributes products/ services that are unrelated with its core business?

1 2 3 4 5

21. Indicate to what extent this strategy improves profitability/ stability of the employer?

1 2 3 4 5

22. Which of those the diversification strategies, improve profitability/ stability of your employer? Explain.

Thank you so much for spending some of your valuable time in answering this questionnaire.

K. O. ABINCHA

RESEARCHER

APENDIX II: LIST OF INSURANCE COMPANIES IN KENYA

1. AAR Insurance Kenya Limited
2. Africa Merchant Assurance Limited Company
3. AIG Kenya Insurance Company
4. APA Insurance Company Limited
5. Apollo Life Insurance Limited
6. British American Insurance Company Limited
7. Cannon Assurance Company Limited
8. Capex Life Assurance Company Limited
9. CFC Life Assurance Company
10. CIC General Insurance Company Limited
11. CIC Life Insurance Company Limited
12. Corporate Insurance Company Limited
13. Directline Assurance Company Limited
14. Fidelity Shield Insurance Company Limited
15. First Assurance Company Limited
16. GA Insurance Company Limited
17. Gateway Insurance Company Limited
18. Geminia Insurance Company Limited
19. Heritage Insurance Company Limited
20. ICEA-Lion General Insurance Company Limited
21. ICEA-Lion Life Assurance Company Limited
22. Intra Africa Assurance Company Limited
23. Invesco Assurance Company Limited
24. Jubilee Insurance Company Limited
25. Kenindia Assurance Company Limited
26. Kenyan Alliance Insurance Company
27. Kenya Orient Insurance Company
28. Madison Insurance Company
29. Mayfair Insurance Company

30. Mercantile Insurance Company Limited
31. Metropolitan Life Insurance Kenya Limited
32. Monarch Insurance Company Limited
33. Occidental Insurance Company Limited
34. Old Mutual Life Assurance Company Limited
35. Pan Africa Life Assurance Company Limited
36. Pacis Insurance Company Limited
37. Phoenix of East Africa Assurance Company Limited
38. Pioneer Life Assurance Company
39. Real Insurance Company
40. Resolution Insurance Company Limited
41. Shield Assurance Company
42. Takaful Insurance of Africa
43. Tausi Assurance Company
44. Trident Insurance Company
45. UAP Insurance Company
46. Xplico Insurance Company Limited