FACTORS INFLUENCING CHOICE OF UNRELATED DIVERSIFICATION STRATEGIES IN THE INSURANCE INDUSTRY IN KENYA

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A MANAGEMENT RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION (MBA), SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI.

NOVEMBER, 2013

DECLARATION

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

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

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

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DEDICATION

I dedicate this project to my dear wife Zipporah Kitheka and my children Faith Kasyoka and Brian Mutuku for their support during the entire period I was working on this project.

ACKNOWLEDGEMENT

The process of this master's management project writing has been a wonderful learning experience in my academic life. It was filled with both challenges and rewards. The completion of my present study leads to a new beginning and a step forward in my endeavors.

I am grateful to God almighty the one above all, who has always been there in my endeavors in life including this study. My profound gratitude goes to my supervisor Professor Peter K'Obonyo and moderator Professor Martin Ogutu for their insightful guidance through the whole process of project writing. Am thankful for the corrections they made on my drafts, their continuous encouragement, support and guidance in writing this project. I am also indebted to my family, my boss at my place of work and friends whom I may not mention in person for their material and moral support which enabled me complete my MBA course successfully.

ABSTRACT

The objective of the study was to determine the factors influencing choice of unrelated diversification strategies in the insurance industry in Kenya. The research design adopted by the study was a survey of insurance companies operating in Kenya. The study used primary data which were collected through self-administered structured questionnaires. The study used primary data which was collected through self-administered questionnaires. The structured questionnaires were used to collect data on the factors influencing the choice of unrelated diversification strategies in the insurance industry in Kenya. The data was analyzed and presented using mean, standard deviation and percentages. Results were presented in tables and charts. The findings of the study was that the reasons for companies pursuing unrelated diversification strategy was the promise for attractive financial gain, availability of resources which makes diversification economically feasible, in order to gain from superior skills of top management people, build shareholder value, profit erosion in maturing markets, in order for the company to reduce risks, in order to increase profitability by exploiting general organization competencies, highly fluctuating industry, in order for the company to learn and the business environment lacking the necessary institutions and factors to compete successfully. The study established that industry profitability, co-insurance effect, firm characteristics and general economic environment influence the insurance companies to pursue unrelated diversification strategies.

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LIST OF ABBREVIATIONS AND ACRONYMS

IRA:	Insurance Regulatory Authority
MIPS:	Medical Insurance Providers

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The increasingly changing business environment, which is characterized by fragmented markets, rapid technological changes and growing dependence on non-price competition, has forced many firms to be innovative in all areas of business activity. The present day customer stresses prompt delivery, unique innovation, and continued optimization of service quality, and all of these are determined by a mechanism that can improve the performance of routine tasks and non-routine projects by enabling the organization personnel to collaborate and optimize processes of collecting, transforming, storing, and sharing the existing knowledge (Grey, 2006). Extensive deregulation, advancements in technology, managerial creativity, and escalating similarity of needs across groups of market participants have led to conditions of convergence (Greenstein, 2000). Convergence increases the substitutive and complementary nature of organizational resources. As a disequilibriating process, convergence causes the blurring of industry and knowledge boundaries inducing lateral entries of firms from adjacent technologies and industries due to the emergence of unanticipated capabilities for which there is little precedent. It perplexes the effectiveness of firms' responses to consumers' needs and creates discontinuities in firms' competitive behavior. These discontinuities present extraordinary strategic challenges for firms to act within dynamic market conditions associated with amplified risk.

The essence of dynamic capabilities in enabling the multi-business firm, irrespective of the firm's coordinates on the diversification continuum, is embedded in organizational processes. Organizational processes are shaped by internal and market resources that the firm possesses such as technology endowments, complementary resources, intellectual property, and customer base (Guillen, 2010). They are conditioned by the evolutionary path the firm has followed that constrains its future behavior. So long as resources are distinctive there is no market for them and they must be built internally (Guillen, 2010).

The value creation potential of unrelated diversification in emerging markets has traditionally been considered as resulted from the market failures and high transaction costs and the opportunities created by the selection environment. Advancing market institutions, coupled with reduced transaction costs and reduced uncertainty, are expected to trigger corporate restructuring, which mostly involves "acquisitions or divestitures to develop a new configuration of the lines of business" (Chung and Luo, 2008 p. 6).

The Kenyan insurance industry has witnessed what can be termed as an exponential growth over the last fifteen years and with only nineteen players in early nineties (IRA,2010) rising to forty four players in year 2012(IRA,2012) . It has grown in both the number of customer base and number of insurance firms to the current forty four insurance firms. As the insurance firms increase, so does the level of competition in more so new players have tended to offer the same products and in most cases adopt similar strategies that players bring to the market have. The competitive strategies have taken the form of price cutting, free promotions and introducing similar product lines. It therefore becomes crucial that the insurance firms come up with different diversification strategies that will give them a greater competitive advantage than other players (IRA 2012). This strategy mix requires action plans to implement, which are closely related to companies' competitive priorities and designed to achieve strategic objectives. Examples of strategies that can be adopted include adopting a low cost strategy, improving the operational efficiencies in the firm's value chain, while an unrelated differentiation strategy that focuses on the customer and providing products and services different from rival products need to be adopted. Unrelated differentiation strategy, therefore, would require action plans either facilitating a quality image or creating a distinct product for the new market environment.

1.1.1 Unrelated Diversification Strategies

Unrelated diversification strategy involves a company's activities outside their industry. According to (Lichtenhaler, 2005) a strategy of unrelated diversification involves diversifying into whatever industries and businesses that hold the promise for attractive financial gain, pursuing strategic fit relationships that assume a back-seat role. In unrelated diversification, the corporate strategy is to diversify into any industry where top management spots a good profit opportunity. The basic premise of unrelated diversification is that any company that can be acquired on good financial terms represents a good business to diversify into. Much time and effort goes into finding and screening acquisition candidates.

Unrelated diversification can also result in superior performance (Datta *et al.,* 2011). Unrelated diversification relies more on the financial and management competencies, which are not necessarily directly related to a company's critical success factors (Montgomery and Singh, 2004). In certain economic environments, unrelated diversification might be a desirable strategy since the environment lacks the necessary institutions and factors to compete successfully. Furthermore, unrelated diversification can be a favorable strategy when the company is facing profit erosion in maturing markets (Datta *et al.,* 2011). Unrelated diversification provides the opportunity to change to industries that are more profitable. In addition, when the firm's primary business is located in a highly fluctuating industry, a company can reduce its risk by diversifying into unrelated businesses.

1.1.2 Insurance Industry in Kenya

The insurance industry is governed by the Insurance Act and regulated by the Insurance Regulatory Authority (IRA). According to IRA annual report (2010) there were 43 insurance companies and 2 locally incorporated reinsurance companies licensed to operate in Kenya. Of the licensed insurance companies, 20 were general insurers, 7 long term insurers and 15 were composite (both life and general) insurers. In addition, there were 201 licensed insurance brokers, 21 medical insurance providers (MIPS), 2,665 insurance agents, 23 loss adjusters, 1 claims settling agent, 213 loss assessors/investigators and 8 risk managers. Insurance industry in Kenya is faced by several challenges that make their operation in the Kenyan market difficult. These challenges are dependent on the people, the status of the market, laws governing insurance in Kenya and the lack of proper information about insurance.

Insurance business in Kenyan has faced challenges ranging from closing down of some firms especially in 1990s and with the closure, many policy holders have ended up losing their investment. In addition, there has been cases where certain genuine claims have not been honored and therefore bringing into disrepute to the industry. Many claims have not been paid due to prolonged investigations to the point that, rather than other insureds' recommending insurance to their friends, they end up discouraging them. Most of those who seek insurance always do so in order to gain the benefit of tax reduction that comes with the package. The Kenyan market is also a young market that is still not well versed with the diversity of the insurance industry because many people are not used to paying premiums in order to alleviate the risks. Most Kenyans therefore consider these rates high and therefore they don't seek insurance. This has been bad for business in the industry as most insurance companies cannot meet their budget and pay claims (IRA, 2012).

Mismanagement of insurance companies is also a challenge that hampers insurance industries in Kenya. Some insurance companies lack proper management due to lack of transparency, which has led to customers losing their money in the process and thus making the public lose trust in the industry. Incompetent management could lead to unrealistically low premiums that make insurance affordable yet not payable. Incompetency is also found in the relay of wrong messages to the public by insurance agents who are often unqualified.

Laws set by parliament to govern the insurance industry have also sometimes failed to meet the unique needs of the third world market. When insurance companies are forced to pay large amounts of money for licenses and that burden is passed to the public, rates are affected. Dishonesty by the public has also hampered insurance business in Kenya, such as by duplication of coverage so as to attempt to realize doubt recoveries. Lack of a big pool of customers has led to problems in realizing the "law of large numbers" on which insurance is predicated. Lack of proper research has led to decision making, especially as to insurability of risks and setting rates and premiums accordingly (IRA, 2012).

1.2 Research Problem

Fierce global competition demonstrates the need for an expanded paradigm to understand how competitive advantage and firm performance is achieved. The competitive behavior of firms often follows a resource-based pattern of mustering valuable technology assets, which is nevertheless insufficient to produce a sustainable competitive advantage (Faccio, 2006). That is because firms often lack the absorptive capacity and dynamic capabilities that can allow them to assimilate knowledge from varying sources and adapt, integrate, and reconfigure internal and external organizational competences and resources to respond to changing environments. Changing environments a rise in external markets due to rival strategic behavior and the emergence of "destructive" technologies or can be fictitiously generated within the firm's boundaries and "internal market" by the firm's diversification strategy. Such evolving and vigorous market environments are very likely to encourage unrelated diversifications.

The insurance industry in Kenya offers almost the same insurance cover thus creating intense competition among the insurance companies and the only distinguishing factor remains to be unrelated diversifications. The introduction of new regulations governing the industry has made the insurance companies to undertake strategic restructuring. However, the nature of strategic change is quite different, as some companies continue to diversify unrelatedly. Although regulations were aimed at the structure and governance of insurance companies, extensive unrelated diversification of insurance companies remains the rule rather than exception and there is no sign that the dominance of these widely diversified groups in the economy will decline.

Studies that have been undertaken on unrelated diversification include Mwindi (2003) studied application of unrelated diversification strategy by the major oil companies in Kenya and established that the concept of non-related diversification as it is applied in the retail networks of Kenyan oil companies lends itself more towards enhancing customer satisfaction than improving the financial performances of the major oil companies. Mwangi (2012) focused on implementation of diversification strategy at the Standard Group (K) Limited and established that the group adopts diversification strategies to maximize profits and compete effectively in the media market; diversification strategies are adopted to consolidate the company's market share and ward off competition from its rivals, so as to spread the risks occasionally by using cost of operation, to maximize on profits. The insurance sector offers the same products to the customers and thus in order to improve their performance they need to diversify. Other studies include Lim and Wang (2007) studied the effect of financial hedging on the incentives for corporate diversification and established that unrelated diversification may partly decrease systematic risk since it involves different industries that are not correlated. In general, financial hedging is less costly compared to unrelated diversification. From the above, there is no study that has been done on the factors influencing choice of unrelated diversification strategies in the insurance industry in Kenya. This study therefore seeks to determine the factors influencing choice of unrelated diversification strategies and it will be guided by the question: what are the factors that influence the choice of unrelated diversification strategies in the insurance industry in Kenya?

1.3 Research Objective

To determine factors influencing choice of unrelated diversification strategies in the insurance industry in Kenya

1.4 Value of the Study

The management of insurance companies will benefit from the study as they will be able to gain more insights concerning the benefits on unrelated diversification and thus pursue the strategy in order to improve their firm performance. The organizations will also be able to reinforce unrelated diversification strategy and capabilities, which in turn will enable such firms to outperform their competitors by creating superior value to their customers. The study will be justified since it will be of academic value to those interested in insurance studies with an aim of establishing a business in the insurance industry since they will be able to understand what to do right to succeed and what if done wrong will bring the business down.

To the government, this research will form an invaluable source of reference especially the ministry of finance in coming out with policies to guide the insurance sector in the diversification strategy. The findings of the study will increase body of knowledge to the scholars in the service industry and make them be in touch with the benefits of diversification strategy.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter is concerned with the review of literature related to the study. An overview of theoretical foundation and factors influencing a company's diversification strategy will be discussed.

2.2 Theoretical Foundation

The resource-based theory provides a rationale for corporate diversification. The type of diversification strategy strongly depends on the resource specificity of the company (Chatterjee and Wernerfelt, 2001). A resource that can only be used in one product is not suitable for diversification into unrelated businesses. In the resource-based approach, resources or capabilities like specialized human capital, technological knowledge, or managerial expertise have the potential to create value when shared across businesses (Miller, 2006). Consequently, the usage of the same resources or capabilities under different circumstances can result in economies of scope and in economic quasi rents, which allows the company to generate sustainable competitive advantage and higher performance. In particular, unique path dependent resources, which are in short supply in the marketplace, can be leveraged across related product lines and provide higher rents. Value is created since these strategic assets are very difficult to imitate or to substitute by other resources (Markides and Williamson, 2006). Besides value creation, a diversified might benefit even more of sharing resources across businesses compared to single focused-firms, since they can use these strategic assets and capabilities among several business units and thereby spreading operating costs among divisions (Markides and Williamson, 2006).

In order to diversify, a company needs to possess the required resources, such that corporate diversification is economically feasible. Chatterjee and Wernerfelt (2001) examined the influence of the degree of flexibility of a resource on the diversification strategy. Three classes of resources were considered in their study: physical resources, intangible assets and, financial resources. The first two of these resources types are rather inflexible, since they are relatively end-product specific. As a result, inflexible resources favor related market diversification. For instance, physical or tangible resources, such as plant and equipment, are highly inflexible, because they only can be used in a few similar industries. Therefore, if a firm has a high degree of excess of physical capacity, it is very likely that the firm will engage in related diversification (Chatterjee and Wernerfelt, 2001). Financial resources have the highest degree of flexibility, and suitable for related and unrelated diversification. However, there is a difference between the effects of the availability of internal funds and equity capital. In general, managers use internal funds for unrelated diversification. However, dependent on the type of risk and the economic environment a company is facing, internal funds may be used for related diversification as well.

The transaction cost theory investigates if a transaction can be undertaken at a lower cost via the market or within the hierarchy of the firm. It consist of the negotiating, monitoring, and enforcements cost which arise when a transaction between two or more parties takes place (Jones and Hill, 2008). The presence of transaction costs causes external motivations for companies to diversify. Six main factors can cause transaction difficulties: bounded rationality, opportunism, uncertainty, small numbers, information impactedness, and asset specificity (Jones and Hill, 2008). Theoretically, in environments where there are no transaction costs, diversification would be a non-value maximization strategy since the resources could be purchased via the market. However, the presence of inefficient markets causes transaction costs, which forces integration. Therefore, the presence of transaction costs is highly dependent on the general economic environment of a country.

An unrelated diversification strategy benefits when it improves the internal capital market of the acquired business. Related diversification focuses on advantages derived from economies of scope (Markides, 2002). Besides the benefit differences between related and unrelated diversification strategies, there also exist transaction costs differences between the two strategies. Discrepancies in bureaucratic costs (monitoring, negotiating, and enforcing) to coordinate and control the separate divisions efficiently, are the main cause of the transaction cost differences. “The main determinant of differences in the bureaucratic costs associated with different strategies arises from organizational interdependencies” (Jones and Hill, 2008). When divisions become jointly specialized and share resources in order to realize economy of scope, it becomes more difficult to monitor and control the performance of each individual division. Therefore, related diversification is the most expensive and difficult strategy to coordinate, since it is associated with reciprocal interdependence. More time, effort, and resources have to be allocated in performance monitoring and evaluation activities within the related diversification strategy. Thus, when interdependency increases, bureaucratic costs increase as well (Jones and Hill, 2008). Bureaucratic costs will be the lowest for unrelated diversification. The organizational structure of unrelated diversified firms is often simple and the different divisions function as self-contained units. As a result, this structure of pooled interdependence allows that performance control can take place based on financial criteria (Jones and Hill, 2008). Consequently, bureaucratic costs of monitoring and controlling the divisions are low.

2.3 Factors Influencing Choice of Unrelated Diversification Strategies

Yu and Pan (2008) posit that the direction of corporate diversification is dependent on several factors. The next section will elaborate on the factors influencing a company’s diversification strategy. As stated in the previous part, this study distinguishes three main factors influencing a company’s unrelated diversification strategy. The first main factor influencing the unrelated diversification strategy is the industry conditions in which the company operates. Industry profitability, foreign-based competition, barriers to entry, and isomorphism are characteristics of the industry. The second factor is co-insurance effect. The third main factor is the characteristics of a firm. This research proposes five firm characteristics: prior-diversification performance, prior diversification size, prior-diversification strategy profile, prior-diversification risk, and prior-diversification resource availability. The last factor is the general economic environment.

2.3.1 Industry Profitability

Industry profitability is a useful indicator of the attractiveness of an industry. When the industry profitability is high, and therefore has high industry attractiveness, manager's desire to stay or enter the industry increases. High-profit industries are often characterized by the presence of firms possessing hard-to-duplicate, firms-specific resources and capabilities (Park, 2002). The resource-based theory state that when the firm possesses hard-to-replicate resources and capabilities, managers have a strong incentive to transfer and exploit these resources and capabilities to other unrelated industries in order to create economies of scope. Companies within profitable industries favor an offensive diversification strategy in order to maintain and strengthen their competitive advantage. The purpose of an offensive diversification strategy is to create value by exploiting and sharing their hard-to-duplicate resources and capabilities across related industries (Yip, 2009). Consequently, managers of firms operating in a high-profit industry tend to favor related diversification over unrelated diversification strategies.

When industry profitability is low, and therefore has low industry attractiveness, managers are more likely to pursue a defensive diversification strategy. The purpose of a defensive diversification strategy is to avoid the unfavorable developments in the firm's current industry by diversifying into industries that are more attractive and have better prospects (Park, 2002). When the company's traditional industry is unattractive, it is very likely that the related industries are unattractive and unprofitable as well. Therefore, firms operating in unattractive low-profit industries seek growth opportunities in other industries by diversifying into unrelated market segments (Park, 2002). Profit erosion in maturing markets, or when the company wants to reduce systematic risk in a highly cyclical industry are examples when companies favor an unrelated diversification strategy over a related diversification strategy.

A company's diversification strategy is also affected by the presence of high entry-barriers. When the barriers to entry are high, newcomers are less inclined to enter this industry. Typically, firm are large within these industries. As a result, industry concentration is high and the degree of monopoly power of a firm increases (Bettis, 2001). According to the market-power theory, monopoly power enables the firms to earn higher profits by raising prices above the competitive level. The higher the entry-barriers of a particular industry, the higher the profit potential a firm can earn (Bettis, 2001). According to Bettis (2001), capital intensity is high in industries characterized by high entry-barriers. Typically, firms within these industries usually require large amount of research and development and advertising expenditures. Furthermore, when investments are sunk costs, firms are less likely to enter that industry, because companies cannot recoup these sunk costs and therefore face a high level of risk. Sunk costs are very product specific and require a long time commitment (Rosenbaum and Lamort, 2007). Since sunk costs involve large firm-specific investments that cannot be recouped, companies are also less likely to exit these industries. Moreover, as in line with the transaction cost theory and resource–based theory, when asset specificity is high, the asset is inflexible and cannot easily be used for other than its primary purpose.

2.3.2 The Co-insurance Effect

Lewellen (2008) states that combining businesses with imperfectly correlated cash flows provides a reduction in operating risk thereby enhancing corporate debt capacity. Lewellen (2008) argues that the increased total borrowing capacity of the merged firm, combined with the effect of tax-deductible interest payments, provides an economic incentive for shareholder wealth-maximizing firms to diversify. By studying a sample of 2,286 firms that engaged in a merger, Kim and McConnell (2007) found that merged firms make greater use of financial merger than the combination of independent firms did before the merger. They state that if the coinsurance effect did not exist they would expect this increase in financial leverage to generate losses for the bondholders of the merging firms. Since they do not find abnormal negative returns for bondholders they conclude that a coinsurance effect did take place. The co-insurance effect has a positive influence on firm debt capacity due to the reduction in the volatility of firm revenues and profits. It is expected this effect to be more intense in firms that develop unrelated diversification strategies because the lack of correlation between businesses is greater. Therefore, co-insurance effect predicts a positive relationship between leverage and the degree of firm diversification.

Singh (2003) argues that, if the co-insurance effect enhances debt capacity and results in increased debt usage for product-diversified firms, it would be reasonable to expect a similar impact for geographically diversified firms, when geographic diversification occurs across political boundaries with imperfectly correlated cash flow streams. Regarding the risk reduction associated with international diversification, Heston and Rouwenhorst (2004) provide evidence that diversification across countries within an industry is a much more effective tool for risk reduction than industry diversification within a country. Fatemi (2006) also provides evidence on the risk-reduction effect of international diversification. By comparing a portfolio of multinational firms with a portfolio of purely domestic firms, he finds that corporate international diversification reduces systematic risk. When analyzing the market's assessment of the net effect of possible higher profits, lower degree of riskiness and the agency costs involved in internationalization, he finds that abnormal returns rise by 18 percent during the 14 months preceding the initial foreign diversification.

2.3.3 Firm Characteristics

Lang and Stulz (2004) posit that it is expected that poor performers diversify into unrelated industries in order to seek for growth opportunities. Therefore, it appears that firms do not become bad performance because they are more diversified, but that they already performed poorly before diversification. For instance, when a company is unprofitable in its core business it will search for markets with better profit potential. However, the company will probably be unprofitable in related businesses as well. Consequently, firms will diversify into unrelated industries to search for growth opportunities. Bowen and Wiersema (2005), argued that well performing firms facing increased competition in its core business, are less inclined to reduce their business diversity. Well performing firms have better financial resources, have greater organizational slack, and are less likely to feel threatened to competitive conditions (Bowen and Wiersema, 2005).

The size and scope of a business group, and its scale in existing industries affect the degree of the business group's unrelated diversification. A firm's previous investments and its repertoire of routines constrain its future behavior (Teece *et al.,* 1997). According to real options framework, investments carry "expansion options" or latent growth opportunities within them, which lower the cost of entry into other product-markets and increase the chances for competing future first-mover-advantages in multiple product-markets. Therefore, the sequential discovery of expansion options can positively affect an organization's diversification performance. The implication of this for business groups in emerging markets is that business groups that expanded into diverse business setting at earlier stages of their development will likely to be advantageous in later years in capitalizing new investment opportunities as they emerge, even if those opportunities are unrelated to their current portfolio.

From an organizational learning perspective, the benefits of larger scope for further unrelated diversification can be explained with reference to "absorptive capacity" arguments. An organization absorptive capacity refers to its ability "to recognize the value of new information, assimilate it, and apply it to commercial ends" (Cohen and Levinhal, 2010: 128). A large scope of a firm implies a broader and more diverse knowledge base, which further increases an organization's absorptive capacity to assimilate market opportunities, and can enhance the firm's capability to further diversify into unrelated product markets. Furthermore, a higher level of absorptive capacity allows a firm to more fully captures the benefits of simultaneous exploitation and exploration (Rothaermel and Alexandre, 2009). Since expansion into similar product lines can be basis for expansion into other product lines, scale and scope typically co-evolve, and scale in existing industries also positively affects the degree of unrelated diversification. Firms can use profits in industries where they have scale advantages to invest in new promising markets or sell those businesses at a higher price to finance their new investments in the promising markets. In other words, businesses with scale advantages can serve as "cash cow" business units to allow unrelated diversification activities as opportunities emerge.

Large firms benefit from organizational slack, which increases the incentives for firms to take risk and pursue unrelated diversification (Dass, 2000). Organizational slack provides the firm the resources necessary to pursue corporate diversification. However, the direction of diversification will depend more on other factors than size. The type of resource the company has in excess, the company's prior-diversification strategy profile, and the risk the company faces will have more impact on the direction of diversification for large firms. These relationships will be explained in the next sections. In contrast, small firms tend to have less organizational slack, which limit their diversification behavior. Moreover, according to the market-power theory, large companies benefit from market power, which allow them to access the necessary resources more easily compared to small firms. Therefore, small organizations often lack the resources, experience, and knowledge to pursue unrelated diversification.

A company's prior-acquisition diversification strategy profile influences a company's diversification strategy. Haleblian *et al.,* (2006) suggests that organizational behavior is guided by routines that stem from prior experience and from performance feedback. When a company has more experience with a strategic action, it increases the likelihood of repeating that action in the future. Over time, the strategic action becomes a routine for the firm. The likelihood of a firm will continuing the same diversification strategy in the future is dependent on the performance feedback outcome of a company's prior diversification strategy (Haleblian et al., 2006). Positive performance feedback increases the likelihood the company will repeat its diversification strategy in the future.
The successful execution of a diversification strategy makes the firm more confident that they have the skills, knowledge and capabilities to be successful in that diversification strategy (Haleblian *et al.,* 2006). Furthermore, repeating a successful diversification strategy is perceived to be less risky than using alternative strategies with limited organizational experience. Therefore, positive performance feedback reinforces the persistency of using a diversification strategy in the future. However, when a company is experiencing negative prior-diversification performance feedback it will explore for alternative strategies (Haleblian et al., 2006). Negative performance feedback challenges the appropriateness and the legitimacy of the diversification strategy and signals the managers to review their diversification program and search for other strategies that improve performance. Therefore, poor performance feedback will reduce a company's motivation to employ the same diversification strategy in the future. Over time, a

company will develop a diversification strategy profile due to the interacting effects of diversification experience, routines, and the performance feedback it receives after a particular strategy.

Managing risk is an important objective of a firm. A company can reduce total risk (systematic risk and firm-specific risk) via financial hedging and via corporate diversification. Financial hedging reduces systematic (market and industry) risk via financial instruments, like future and options contracts. A conflict of interests may arise between shareholders and non-financial stakeholders when reducing total risk. Both the shareholders and the non-financial stakeholders want to reduce systematic risk and firm-specific risk. To buffer against fluctuation in firm-specific risk, shareholders diversify firm-specific risk by holding a diversified portfolio of stocks from different companies operating in different markets and industries. Because the shareholders can reduce firm-specific risk, they encourage investments in firm-specific assets, since it raises the value of the firm and their stock value (Amihud and Lev, 2001). However, non-financial stakeholders are concerned with the risk associated with firm-specific investments, because they cannot diversify away this firm-specific risk (Wang and Barney, 2006). Therefore, these stakeholders are reluctant to invest in firm-specific assets. Consequently, firm-specific risk will be a function of total risk (systematic and firm-specific risk), since non-financial stakeholders cannot diversify firm-specific risk. As a result, when a firm can reduce total risk, the stakeholders are more willing to invest in firm-specific investments (Lim and Wang, 2007).

Unrelated diversification may partly decrease systematic risk since unrelated diversification involves different industries that are not correlated. In general, financial hedging is less costly compared to unrelated diversification (Lim and Wang, 2007). When financial hedging is effective in reducing industry-wide risk and market-wide risk, it decreases the need for unrelated diversification (Lim and Wang, 2007). However, when financial hedging is less effective in decreasing industry-wide risk than in reducing market-wide risk, financial hedging increases the need for unrelated diversification (Lim and Wang, 2007).

Managers prefer unrelated diversification, since they are not able to diversify their employment risk. This is in line with the agency theory, which argues that managers may work in their self-interest in order to maximize their payoff. Several explanations exist for the motives why managers diversify for their self-interest. Prestige and power associated with leading a large diversified firm encourage managers to behave in their self-interest. Managerial risk reduction is another often-cited reason for diversification. Typically, managers hold large, undiversified positions within their own firm (Aggarwal and Samwick, 2003). Shareholders can efficiently diversify their stock portfolio in order to reduce their total investment risk. In contrast, “managers cannot so efficiently diversify their employment risk” (Montgomery, 2004). To reduce the systematic risk, managers may pursue diversification strategies that are not in the shareholders interests. However, the incentive of managers to behave in their self-interest is heavily dependent on the ownership structure of the firm (Denis *et al.,* 2009). When outside shareholders are more concentrated, there is a larger incentive to monitor managers’ behavior. As a result, managers will act more in favor of the shareholders’ interests (Denis *et al.,* 2009).

2.3.4 General Economic Environment

Industry conditions and organizational characteristics vary with fluctuations in the general economic environment of a country. The study of Dubofsky and Varadarajan (2007) showed that mixed performance outcomes between related and unrelated diversification might be largely attributed to differences in the economic conditions among countries. The study of Ramanujam and Varadarajan (2009) acknowledged that the general economic environment has an effect on a company’s decision to diversify. However, their study did not investigate the impact of the general economic environment on the direction of diversification. Furthermore, Hoskisson and Hill (2010) suggested that changes in tax laws and fluctuations in interest rates explained the presence of related and unrelated diversifiers from the 1990s until the 2000s. Hoskisson and Hill (2010) argued that motivations for unrelated diversification were mainly based on the tax advantages it received from diversification.

The general economic environment is strongly influenced by the availability of resources and the presence of institutions. Since the availability of resources and institutions have a significant impact on a company's strategy, it also influences the choice and the direction of corporate diversification. The degree of resources and institutions in a country is measured by the level of environmental munificence. Environmental munificence can be described as "the availability of crucial factors and institutions in a home country environment" (Wan and Hoskisson, 2003, p.29). Factors, which are more tangible, can be classified into endowed factors (natural resources), advanced factors (physical infrastructure, financial resources, and capital goods accumulation), and human factors (labor quality, education). Obviously, firms need these resources in order to grow. Institutions are less tangible and can be divided into political institutions, legal institutions and societal institutions (Wan and Hoskisson, 2003). Institutions are responsible of an efficient and well functioning of the external market. Countries differ in the availability of factors and institutions. Therefore, variations in the degree of environmental munificence will influence a company's diversification strategy, since different opportunities and constraints are available to the company.

Environments with a high level of munificence, firms benefit from an abundant supply of factors and institutions. In these environments, physical infrastructure, labor market, and financial markets are well developed. Since obtaining resources can be relatively easy, firms place greater emphasis on best utilizing these resources (Wan, 2005). Therefore, competitive advantage is created by forming specialized resources and skills. In order to avoid a deterioration of a firm's market position, the source of competitive advantage rest on continuously improvement of a firm's core strategic assets (Wan, 2005). In order to benefit from economies of scope and stay on the competitive edge, related diversification permit managers to allocate more attention to a small number of related products markets (Wan, 2005). Furthermore, in high environmental munificence environments, institutions are well developed. In a high munificence environment, unrelated diversification may be a relatively undesirable strategy because the source of competitive advantage in those industries rest on developing and continuously improving strategic assets. Therefore, environments characterized by a high level of munificence favor related diversification over unrelated diversification.

In less munificence environments, like emerging economies, there is a shortage of crucial factors and institutions are lacking. These economies are characterized by inadequate transaction mechanisms, which increase incentives for companies to control its activities internally (Wan, 2005). For example, in high munificence environments firms can reduce the market risk by using financial hedging instruments. However, in less munificence environments, financial markets are ineffective, which encourage companies to engage in unrelated diversification strategies to reduce risk. Furthermore, the absence of proper antitrust enforcements and inadequate legal institutions increase the transaction costs via the market. As a result, companies pursue an unrelated diversification strategy in order to better control and sanction opportunistic behavior (Lincoln *et al.,* 1996). This may explain the higher concentration of unrelated diversifiers in emerging economies.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The chapter describes the proposed research design, the target population, data collection instruments and the techniques for data analysis.

3.2 Research Design

The research design adopted was a cross sectional survey design. According to Cooper and Schindler (2000), a descriptive research design is concerned with finding out the; who, what, where, when and how much. Furthermore, a research design is structured, has investigative questions and part of formal studies. The design is appropriate because the main interest is to explore the viable relationship and describe how the factors support matters under investigation.

A cross sectional study looks at data collected across a whole population to provide a snapshot of that population at a single point in time. This kind of study was used to determine the factors influencing choice of unrelated diversification strategies in the insurance industry in Kenya. Descriptive design method provides quantitative data from cross section of the chosen population. This design provided further insight into research problem by describing the variables of interest.

3.3 Target Population

The population of the study comprised all insurance companies operating in Kenya (Appendix II). According to the (IRA, 2012), there are forty four (44) insurance companies in Kenya and all of them participated, hence the study was a census (see attached list of the forty four (44) insurance companies in Kenya).

3.4 Data Collection

The study used primary data which was collected through self-administered questionnaires. The structured questionnaires were used to collect data on the factors influencing the choice of unrelated diversification strategies in the insurance industry in Kenya. The questionnaires consisted of both open and closed ended questions designed to elicit specific responses for qualitative and quantitative analysis, respectively. The questionnaire was administered through "drop and pick later" method. The questionnaire was divided into three sections. Section A dealt with the demographic data, section B dealt with unrelated diversification strategies while Section C dealt with factors influencing the choice of unrelated diversification strategies.

3.5 Data Analysis

The data collected was analyzed using descriptive statistics (measures of central tendency and measures of variations). Once the data is collected, the questionnaires were edited for accuracy, consistency and completeness. However, before final analysis is performed, data was cleaned to eliminate discrepancies and thereafter, classified on the basis of similarity and then tabulated. The responses were then coded into numerical form to facilitate statistical analysis. Data was analyzed using statistical package for social sciences based on the questionnaires. In particular mean scores, standard deviations, percentages and frequency distribution was used to summarize the responses and to show the magnitude of similarities and differences. Results were presented in tables and charts.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

The research objective was to establish the factors influencing choice of unrelated diversification strategies in the insurance industry in Kenya. This chapter presents the analysis and findings with regard to the objective and discussion of the same. The findings are presented in percentages and frequency distributions, mean and standard deviations. A total of 44 questionnaires were issued out. The completed questionnaires were edited for completeness and consistency. Of the 44 questionnaires issued out, only 39 were returned. This represented a response rate of 89%.

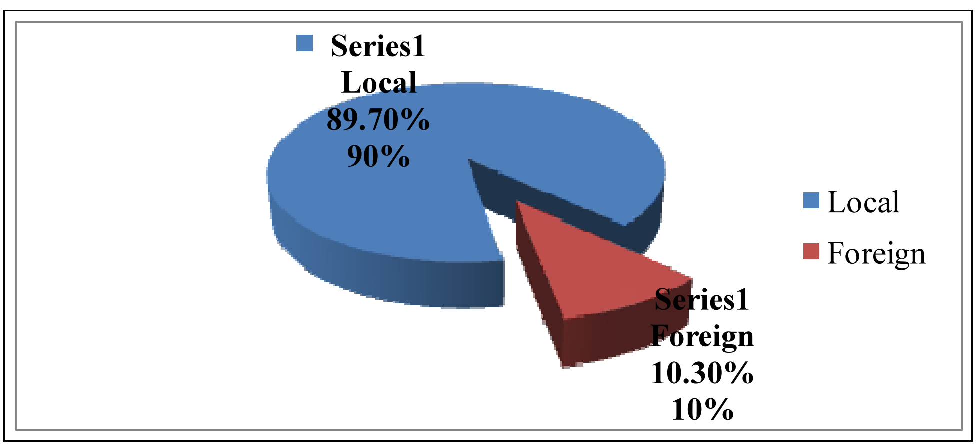
4.2 Demographic Information

The demographic information considered in this study were ownership of insurance company, length of continuous service with the insurance company, number of employees in the company and duration of insurance company existence.

4.2.1 Insurance Company Ownership

The respondents were requested to indicate the ownership of the insurance company. The results are presented in figure 4.1.

Figure 4.1: Composition of Ownership



The results indicate that 89.7% of the insurance companies operating in Kenya are owned by the locals while 10.3% of the companies are owned by foreigners. The results indicate that the presence of foreign insurance companies gives rise to high competition in the industry which necessitates unrelated diversification in order to improve the firm profitability.

4.2.2 Length of Continuous Service

The respondents were asked to indicate the duration they have continuously worked in the company and the results are presented in table 4.1

Table 4.1: Employee Length of Continuous Service

Years of Continuous Service	Frequency	Percentage	Cumulative percentage
Less than 5	16	41.0	41.0
5-10	6	15.4	56.4
Over 10	17	43.6	100.0
Total	39	100.0	

The results in table 4.1 indicate that 43.6% of the respondents have worked in the company for a period of over 10 years, 41% of the respondents said that they have worked in the company for less than 5 years while 15.4% of the respondents indicated that they have worked for a period of between 5 and 10 years. The duration in which the respondents have worked in the company is sufficient for them to give information on the company unrelated diversification strategy.

4.2.3 Number of Employees

The respondents were asked to indicate the number of employees in their company and the results are presented in table 4.2

Table 4.2: Number of Employees

Number of Employees	Frequency	Percent	Cumulative percent
100 – 499	19	48.7	48.7
Above 500	20	51.3	100.0
Total	39	100.0	

Table 4.2 indicates that 48.7% of the companies had employees ranging from 100 to 499 while 51.2% of companies have more than 500 employees. The number of employees in the companies is over 100, an indication that the companies are large in size and thus needs more employees in order to achieve their objectives.

4.2.4 Duration of Insurance Company Existence

The respondents were asked to indicate the duration in which the insurance companies have been in existence.

Table 4.3: Years of Company Operations

Years of Existence	Frequency	Percent	Cumulative percent
Under 5	3	7.7	7.7
6 – 10	5	12.8	20.5
Over 15	31	79.5	100.0
Total	39	100.0	

As shown in table 4.3, number of years of service indicates that 79.5% of the companies have been in existence for over 15 years, 12.8% of the companies have been in existence for a period of 6 to 10 years while 7.7% of the companies have been in existence for less than 5 years. The duration and the number of companies in the country contribute to the companies' unrelated diversification strategies in order to improve their financial gains.

4.3 Unrelated Diversification Strategies

Unrelated diversification involves diversifying into whatever industries and businesses that hold the promise for attractive financial gain, pursuing strategic fit relationships that assume a back-seat role. The findings on the adoption of unrelated diversification by the companies was that all the companies have adopted unrelated diversification strategy and this will enable the companies to use the same resources or capabilities thus resulting in economies of scope and in economic quasi rents, which allows the company to generate sustainable competitive advantage and higher performance.

4.3.1 Factors that Influenced Adoption of Unrelated Diversification Strategies

The respondents were requested to indicate the factors that influence the adoption of unrelated diversification strategies in a five point Likert scale. The range was ‘not at all (1)’ to ‘very great extent’ (5). The scores of not at all have been taken to represent a variable which had mean score of 0 to 2.5 on the continuous Likert scale; (0≤ S.E <2.4). The scores of ‘moderate’ have been taken to represent a variable with a mean score of 2.5 to 3.4 on the continuous Likert scale: (2.5≤ M.E. <3.4) and the score of both great extent and very great extent have been taken to represent a variable which had a mean score of 3.5 to 5.0 on a continuous Likert scale; (3.5≤ L.E. <5.0). A standard deviation of >0.9 implies a significant difference on the impact of the variable among respondents. The results are presented in Table 4.4.

Table 4.4: Reasons for Adopting Unrelated Diversification Strategies

Reasons for adopting unrelated diversification Strategies	Mean	Std. Deviation
In order to hold the promise for attractive financial gain	4.0769	.8393
The business environment lacks the necessary institutions and factors to compete successfully	3.5128	.7904
The company is facing profit erosion in maturing markets	3.8718	.8938
In order to increase profitability by exploiting general organization competencies	3.7436	.9380
The firm's primary business is located in a highly fluctuating industry	3.6333	.7374
In order for the company to reduce risks	3.7897	.8801
The company possesses the required resources, such that corporate diversification is economically feasible	4.0256	1.0127
In order to gain from superior skills of top management people	3.9907	1.0461
Building share-holder value	3.8974	.9945
For organizational learning	3.5641	1.0207

The insurance companies adopt unrelated diversification strategies due to the promise for attractive financial gain (mean 4.0769), the company possesses the required resources, such that corporate diversification is economically feasible (mean 4.0256), in order to gain from superior skills of top management people (mean 3.9907), build shareholder value (mean 3.8974), when the company is facing profit erosion in maturing markets (mean 3.8718), in order for the company to reduce risks (mean 3.7897), in order to increase profitability by exploiting general organization competencies (mean 3.7436), the primary business of the insurance company being located in a highly fluctuating industry (mean 3.6333), in order for the company to learn (3.5641) and the business environment lacking the necessary institutions and factors to compete successfully (mean 3.5128). The results indicate that the insurance companies' pursuit of unrelated diversification strategies differs. The low variation of standard deviation indicates that the respondents were unanimous on the reasons behind the adoption of unrelated diversification strategies by the insurance companies in Kenya.

4.4 Factors Influencing Choice of Unrelated Diversification Strategies

An unrelated diversification strategy benefits when it improves the internal capital market of the acquired business. The direction of corporate diversification is dependent on the industry profitability, co-insurance effect, firm characteristics and the economic environment. The results are presented in a five point Likert scale. The range was 'not at all (1)' to 'very great extent' (5). The scores of not at all have been taken to represent a variable which had mean score of 0 to 2.5 on the continuous Likert scale; (0≤ S.E <2.4). The scores of 'moderate' have been taken to represent a variable with a mean score of 2.5 to 3.4 on the continuous Likert scale: (2.5≤ M.E. <3.4) and the score of both great extent and very great extent have been taken to represent a variable which had a mean score of 3.5 to 5.0 on a continuous Likert scale; (3.5≤ L.E. <5.0).

4.4.1 Industry profitability

The respondents were asked to indicate the effect of industry profitability on company's unrelated diversification Strategy.

Table 4.5: Response on Industry Profitability

Industry profitability	Mean	Std. Deviation
The industry profitability is high, and therefore has high industry attractiveness, manager's desire to stay or enter the industry increases	3.2821	.8255
The company possesses hard-to-duplicate, firms-specific resources and capabilities	3.2051	.7319
The company pursue unrelated diversification strategies in order to create economies of scope	4.2821	.6468
The company pursue unrelated diversification strategies due to profit erosion in maturing markets	4.1282	.8938
The company seek growth opportunities in other industries due to unattractive low-profit industry	3.7128	.8544

The insurance companies adopted unrelated diversification strategies as a result of the need to create economies of scope (mean 4.2821), due to profit erosion in maturing markets (mean 4.1282) and the need by the company to seek growth opportunities in other industries due to unattractive low-profit industry (mean 3.7128). The industry profitability being high and therefore has high industry attractiveness, manager's desire to stay or enter the industry increases (mean 3.2821) and the possession by the companies of hard-to-duplicate, firms-specific resources and capabilities (mean 3.2051) influenced the adoption of unrelated diversification strategies by the companies to a moderate extent. The results indicate that the industry profitability influenced the adoption of unrelated diversification strategies and this was also confirmed by the low standard deviation variation.

4.4.2 Co-insurance Effect

The results in table 4.6 indicate the co-insurance effect on the company's adoption of unrelated diversification strategy.

Table 4.6: Influence of Co-insurance Effect

Influence of co-insurance effect	Mean	Std. Deviation
The company diversify due to increased total borrowing capacity combined with the effect of tax-deductible interest payments	2.7179	.7930
The company diversifies due to co-insurance effect that has a positive influence on the company debt capacity due to the reduction in the volatility of firm revenues and profits	3.6872	.8230
The co-insurance effect enhances debt capacity and results in increased debt usage for product-diversified firms	3.8385	.9691

The findings indicate that the co-insurance effect enhances debt capacity and results in increased debt usage for product-diversified firms (mean 3.8385) and the co-insurance effect that has a positive influence on the company debt capacity due to the reduction in the volatility of firm revenues and profits (mean 3.6872). The insurance companies were however influenced by increased total borrowing capacity combined with the effect of tax-deductible interest payments (mean 2.7179) to a moderate extent. The low variation in standard deviation indicates the effect of the factors on the insurance companies' adoption of unrelated diversification.

4.4.3 Firm Characteristics

The results in table 4.7 indicate the influence of firm characteristics on the insurance companies' adoption of unrelated diversification strategy.

Table 4.7: Influence of Firm Characteristics

Influence of firm characteristics	Mean	Std. Deviation
The company seek for growth opportunities	4.8974	.30735
The size and scope of a business group, and its scale in existing industries	3.8974	.94018
Lower cost of entry into other product-markets and increase the chances for competing future first-mover-advantages in multiple product-markets	3.5128	.91398
Capitalizing new investment opportunities	4.7692	.53614
The company want to benefit from a larger scope which broadens their knowledge base thus increased absorptive capacity to assimilate market opportunities	4.1538	.81235
The company has a higher level of absorptive capacity that allows it to more fully captures the benefits of simultaneous exploitation and exploration	3.6154	.93514
The company uses profits in industries where they have scale advantages to invest in new promising markets or sell those businesses at a higher price to finance their new investments in the promising markets	3.9231	.89984
The company benefit from organizational slack, which increases the incentives for firms to take risk and pursue unrelated diversification	3.5333	.80568
The company has a positive performance feedback that reinforces the persistency of using a diversification strategy in the future	3.6667	1.05963
The managers undertake the diversification since they are not able to diversify their employment risk	2.1026	.91176

The adoption of unrelated diversification strategies by the insurance companies was influenced by the company need to seek for growth opportunities (mean 4.8974), capitalizing on new investment opportunities (mean 4.7692), the need by the company to benefit from a larger scope which broadens their knowledge base thus increased absorptive capacity to assimilate market opportunities (mean 4.1538), the use of profits by the company in industries where they have scale advantages to invest in new promising markets or sell those businesses at a higher price to finance their new investments in the promising markets (mean 3.9231), the size and scope of a business group, and its scale in existing industries (mean 3.8974), the company has a positive performance feedback that reinforces the persistency of using a diversification strategy in the future (mean 3.6667), the company has a higher level of absorptive capacity that allows it to more fully captures the benefits of simultaneous exploitation and exploration (mean 3.6154), the benefit of the companies from organizational slack, which increases the incentives for firms to take risk and pursue unrelated diversification strategies (mean 3.5333) and lower cost of entry into other product-markets and increase the chances for competing future first-mover-advantages in multiple product-markets (mean 3.5128). The companies however do not undertake unrelated diversification strategies due to managers being unable to diversify their employment risk (2.1026).

4.4.4 General Economic Environment

The results on the influence of the general economic environment on the insurance companies' unrelated diversification are shown in table 4.8 below.

Table 4.8: Influence of General Economic Environment

Influence of general economic environment	Mean	Std. Deviation
The company adopt unrelated diversification due to changes in tax laws and fluctuations in interest rates	1.9231	.92863
The company adopt the diversification due to the availability of resources and institutions as they significantly impact on a company's strategy	3.7436	.81815
The degree of environmental munificence will influence a company's diversification strategy, since different opportunities and constraints are available to the company	3.8718	.80064

The company pursue an unrelated diversification strategy in order to better control and sanction opportunistic behavior	3.8205	1.02268

The findings indicate that the insurance companies pursue unrelated diversification as a result of environmental munificence which influence a company's diversification strategy, since different opportunities and constraints are available to the company (mean 3.8718), in order to better control and sanction opportunistic behavior (mean 3.8205), due to the availability of resources and institutions as they significantly impact on a company's strategy (mean 3.7436). The results indicate that the companies do not undertake unrelated diversification due to changes in tax laws and fluctuations in interest rates. The results indicate that the economic environment influences the insurance companies' decision to diversify to unrelated business.

4.5 Discussion of the Findings

The objective of the study was to establish the factors influencing the choice of unrelated diversification strategies in the insurance industry in Kenya. The findings from the study indicate that the insurance industry has been employing unrelated diversification strategies which have led to their success in their operations. The results were consistent with Lichtenhaler (2005) findings that unrelated diversification involves diversifying into whatever industries and businesses that hold the promise for attractive financial gain, pursuing strategic fit relationships that assume a back-seat role. The corporate strategy is to diversify into any industry where top management spots a good profit opportunity. In certain economic environments, unrelated diversification might be a desirable strategy since the environment lacks the necessary institutions and factors to compete successfully. Furthermore, unrelated diversification can be a favorable strategy when the company is facing profit erosion in maturing markets (Datta *et al.,* 2011).

It has been found that the reasons for companies pursuing unrelated diversification strategies is the promise for attractive financial gain, availability of resources which makes diversification economically feasible, in order to gain from superior skills of top management people, build shareholder value, profit erosion in maturing markets, in order for the company to reduce risks, in order to increase profitability by exploiting general organization competencies, highly fluctuating industry, in order for the company to learn and the business environment lacking the necessary institutions and factors to compete successfully. Moreover industry profitability, co-insurance effect, firm characteristics and general economic environment influence the insurance companies to pursue unrelated diversification strategies. The findings were consistent with Yu and Pan (2008) findings that the direction of unrelated diversification strategy is influenced by industry conditions in which the company operates. Industry profitability, foreign-based competition, barriers to entry, and isomorphism are characteristics of the industry, the co-insurance effect, characteristics of a firm. The study also established that the co-insurance effect also influenced unrelated diversification which led to increased debt usage for product-diversified firms. This was in line with Lewellen (2008) findings that combining businesses with imperfectly correlated cash flows provides a reduction in operating risk thereby enhancing corporate debt capacity.

The findings have differed on the previous studies that have been undertaken on unrelated diversification strategies by Mwindi (2003) on major oil companies in Kenya which found that application of unrelated diversification strategies by the major oil companies in Kenya led to enhancing customer satisfaction rather than improving the financial performances.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary of the Findings

The study shows that majority of the insurance companies are locally owned while a few are foreign owned and this would give rise to intense competition in the industry which has resulted in all the insurance companies pursuing unrelated diversification strategies in order to improve the firm profitability. The respondents have worked in the company for a longer duration of time and thus understand the need for the insurance firms to pursue unrelated diversification strategies. The results indicate that most of the insurance companies have been in operation for a longer duration of time and thus they understand the dynamics of the Kenyan market and this could have driven them to pursue other unrelated businesses.

The study established that the reasons advanced by the companies for adopting unrelated diversification strategies was the promise for attractive financial gain, availability of resources which makes unrelated diversification economically feasible, in order to gain from superior skills of top management people, build shareholder value, profit erosion in maturing markets, in order for the company to reduce risks, in order to increase profitability by exploiting general organization competencies, highly fluctuating industry, in order for the company to learn and the business environment lacking the necessary institutions and factors to compete successfully. The study established that industry profitability, co-insurance effect, firm characteristics and general economic environment influence the insurance companies to pursue unrelated diversification. The industry profitability factors that contributed to the insurance companies' pursuit of unrelated diversification are the need to create economies of scope, due to profit erosion in maturing markets and the need by the company to seek growth opportunities in other industries due to unattractive low-profit industry.

The study also established that the co-insurance effect influenced unrelated diversification by the insurance firms and these was as a result of debt enhancement capacity that increased debt usage for product-diversified firms and the co-insurance effect that has a positive influence on the company debt capacity due to the reduction in the volatility of firm revenues and profits. The characteristics of the insurance companies was also established to influence unrelated diversification as it assists for growth opportunities, capitalizing on new investment opportunities, broadening of knowledge base thus increased absorptive capacity to assimilate market opportunities, use of profits to invest in new promising markets or sell those businesses at a higher price to finance their new investments in the promising markets, the size and scope of a business group, and its scale in existing industries, positive performance feedback that reinforces the persistency of using a diversification strategy in the future, higher level of absorptive capacity that allows it to more fully captures the benefits of simultaneous exploitation and exploration, the benefit from organizational slack, which increases the incentives for firms to take risk and pursue unrelated diversification and lower cost of entry into other product-markets and increase the chances for competing future first-mover-advantages in multiple product-markets.

The economic environment factors that influenced insurance companies to pursue unrelated diversification was found to be environmental munificence since different opportunities and constraints are available to the company, in order to better control and sanction opportunistic behavior, due to the availability of resources and institutions as they significantly impact on a company's strategy. The results indicate that the pursuant of unrelated diversification strategy by the insurance companies was in harmony with both resource based view and the transaction cost theory. According to the resource-based view, a company should leverage its strategic assets and core competences among its businesses in order to realize economies of scope. Furthermore, the resource-based theory demonstrates that the company needs to possess essential resources in order to make diversification economically feasible. Therefore, the direction of corporate diversification is dependent on the type of resource availability. The transaction cost theory explains the rationale for a firm to execute a transaction internally or via the market. However, transaction costs are very dependent on the general economic environment in which the company is located.

5.2 Conclusion

Based on the objectives and the research questions it was possible to conclude that the insurance industry in Kenya adopted unrelated diversification strategies. It can be concluded that majority of the insurance companies are locally owned while a few are foreign owned giving rise to intense competition in the industry which resulted in all the insurance companies pursuing unrelated diversification strategies in order to improve the firm profitability. The Insurance companies adopted unrelated diversification strategies as a promise for attractive financial gain, availability of resources which made unrelated diversification economically feasible, superior skills of top management people and building shareholder value. The study established that industry profitability, co-insurance effect, firm characteristics and general economic environment influenced the insurance companies to pursue unrelated diversification.

The characteristics of the insurance companies was also established to have influenced unrelated diversification as it assisted growth opportunities, capitalizing on new investment opportunities, broadening of knowledge base thus increased absorptive capacity to assimilate market opportunities and use of profits to invest in new promising markets or sell those businesses at a higher price to finance their new investments in the promising markets. The economic environment factors influenced insurance companies to pursue unrelated diversification since different opportunities and constraints were available to the companies, better control and opportunistic behavior, availability of resources and institutions as they significantly impacted on a company’s strategy.

5.3 Recommendations

Insurance companies in Kenya and other organizations should pursue unrelated diversification strategies which businesswise is health as business risks are spread over different industries. Capital resources are effectively allocated bringing back stable profits and even enhanced shareholder value. Emerging attractive unrelated business opportunities can only be utilized through the application of unrelated diversification strategies which increases shareholders’ financial gains.

5.4 Suggestions for Further Research

Since the researcher focused only on the factors influencing unrelated diversification strategies in the insurance industry in Kenya, it is not possible to generalize the findings of the study to others financial sectors like the banking industry in Kenya. The unrelated diversification strategies employed by the insurance industry in Kenya could be different from those employed by the banking industry in Kenya. A similar research should be conducted on the banking industry in Kenya.

5.5 Limitation of the Study

The study findings accuracy was limited to the extent to which best respondents' were not available to respond to the questionnaires. Best response was expected to come from the chief executive officers who were very difficult to get their views forcing the researcher to seek information from other middle level managers. Given the sensitive nature of the data collected, there may have been likelihood of answering questions in a certain way so as to avoid giving away crucial and confidential strategic secrets that could be used by the competitors to gain competitive advantage. Failure to get 100% response rate could mean that some information vital in determining the factors leading to choice of unrelated diversification strategies were not given.

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APPENDICES

Appendix I: Questionnaire

Please give answers in the spaces provided and tick (√) the box that matches your response to the questions where applicable.

Part A: Demographic Profile

1. Name of the Insurance company : --

2. How is the ownership of insurance company you work for?

   Local ( ) Foreign ( )

3. Length of continuous service with the insurance company?

   a) Less than five years ( )
   b) 5-10 years ( )
   c) Over 10 years ( )

4. How many employees are there in your insurance company?

   a) Less than 100 ( )
   b) 100 – 499 ( )
   c) Above 5000 ( )

5. For how long has your insurance company been in existence?

   a) Under 5 years ( )
   b) 6 – 10 years ( )
   c) Over 25 years ( )

Part B: Unrelated Diversification Strategies

6. Has your company adopted unrelated diversification strategy?

   Yes ( ) No ( )

7. To what extent did the following factors influenced your company to adopt unrelated diversification strategy? Use 1-Not at all, 2-Small extent, 3-Moderate extent, 4-Great extent and 5-Very great extent.

Reasons for diversification	1	2	3	4	5
Diversification into whatever industries and businesses that hold the promise for attractive financial gain					
The business environment lacks the necessary institutions and factors to compete successfully					
The company is facing profit erosion in maturing markets					
Increasing Profitability by exploiting general organization competencies					
The firm's primary business is located in a highly fluctuating industry					
In order for the company to reduce risks					
The company possesses the required resources, such that corporate diversification is economically feasible.					
The company adopt unrelated diversification in order to gain from superior skills of top management people					
Building share-holder value					
The company pursue unrelated diversification for organizational learning					

Part C: Factors Influencing Choice of Unrelated Diversification Strategies

A) Industry Profitability

8. To what extent did the industry profitability influenced your company to pursue unrelated diversification strategy? Use 1-Not at all, 2-Small extent, 3-Moderate extent, 4-Great extent and 5-Very great extent.

Profitability factors	1	2	3	4	5
The industry profitability is high, and therefore has high industry attractiveness, manager's desire to stay or enter the industry increases					
The company possesses hard-to-duplicate, firms-specific resources and capabilities					
The company pursue unrelated diversification in order to create economies of scope					
The company pursue unrelated diversification due to profit erosion in maturing markets					
The company seek growth opportunities in other industries due to unattractive low-profit industry					

B) The Co-insurance Effect

9. To what extent did the following co-insurance effect influenced your company decision to undertake unrelated diversification strategy? Use 1-Not at all, 2-Small extent, 3-Moderate extent, 4-Great extent and 5-Very great extent.

Co-insurance effect	1	2	3	4	5
The company diversify due to increased total borrowing capacity combined with the effect of tax-deductible interest payments					
The company diversifies due to co-insurance effect that has a positive influence on the company debt capacity due to the reduction in the volatility of firm revenues and profits.					
The co-insurance effect enhances debt capacity and results in increased debt usage for product-diversified firms					

C) **Firm Characteristics**

10. To what extent did the following firm characteristics influenced your company decision to undertake unrelated diversification strategy? Use 1-Not at all, 2-Small extent, 3-Moderate extent, 4-Great extent and 5-Very great extent.

Firm characteristics	1	2	3	4	5
The company seek for growth opportunities					
The size and scope of a business group, and its scale in existing industries					
lower cost of entry into other product-markets and increase the chances for competing future first-mover-advantages in multiple product-markets					
capitalizing new investment opportunities					
The company want to benefit from a larger scope which broadens their knowledge base thus increased absorptive capacity to assimilate market opportunities					
The company has a higher level of absorptive capacity that allows it to more fully captures the benefits of simultaneous exploitation and exploration					
The company uses profits in industries where they have scale advantages to invest in new promising markets or sell those businesses at a higher price to finance their new investments in the promising markets.					
The company benefit from organizational slack, which increases the incentives for firms to take risk and pursue unrelated diversification					
The company has a positive performance feedback that reinforces the persistency of using a diversification strategy in the future					
The managers undertake the diversification since they are not able to diversify their employment risk.					

D) General Economic Environment

11. To what extent did general economic environment influenced your company decision to undertake unrelated diversification strategy? Use 1-Not at all, 2-Small extent, 3-Moderate extent, 4-Great extent and 5-Very great extent.

General economic environment factors	1	2	3	4	5
The company adopt unrelated diversification due to changes in tax laws and fluctuations in interest rates					
The company adopt the diversification due to the availability of resources and institutions as they significantly impact on a company's strategy					
The degree of environmental munificence will influence a company's diversification strategy, since different opportunities and constraints are available to the company					
The company pursue an unrelated diversification strategy in order to better control and sanction opportunistic behavior					

Appendix II: List of Insurance Firms in Kenya

No.	Insurance Company Name
1.	AAR Insurance Kenya Limited
2.	A P A Insurance Limited
3	Africa Merchant Assurance Company Limited
4.	Apollo Life Assurance Limited
5.	AIG Kenya Insurance Company Limited
6.	British-American Insurance Company (Kenya) Limited
7.	Cannon Assurance Limited
8.	Capex Life Assurance Company Limited
9.	CFC Life Assurance Limited
10.	CIC General Insurance Limited
11.	CIC Life Assurance Limited
12.	Corporate Insurance Company Limited
13.	Directline Assurance Company Limited
14.	Fidelity Shield Insurance Company Limited
15.	First Assurance Company Limited
16.	G A Insurance Limited,
17.	Gateway Insurance Company Limited
18.	Geminia Insurance Company Limited
19.	ICEA LION General Insurance Company Limited
20.	ICEA LION Life Assurance Company Limited
21.	Intra Africa Assurance Company Limited
22.	Invesco Assurance Company Limited
23.	Kenindia Assurance Company Limited
24.	Kenya Orient Insurance Limited
25.	Madison Insurance Company Kenya Limited
26.	Mayfair Insurance Company Limited
27.	Mercantile Insurance Company Limited
28.	Metropolitan Life Insurance Kenya Limited

29. Occidental Insurance Company Limited
30. Old Mutual Life Assurance Company Limited
31. Pacis Insurance Company Limited
32. Pan Africa Life Assurance Limited
33. Phoenix of East Africa Assurance Company Limited
34. Pioneer Assurance Company Limited
35. Real Insurance Company Limited
36. Shield Assurance Company Limited
37. Takaful Insurance of Africa Limited
38. Tausi Assurance Company Limited
39. The Heritage Insurance Company Limited
40. The Jubilee Insurance Company of Kenya Limited
41. The Monarch Insurance Company Limited
42. Trident Insurance Company Limited
43. UAP Insurance Company Limited
44. UAP Life Assurance Limited