

**THE EFFECT OF INVESTMENT STRATEGIES ON THE FINANCIAL PERFORMANCE OF
COLLECTIVE INVESTMENT SCHEMES IN KENYA**

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DECLARATION

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

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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 work to my husband; Kimathi and my children; Makena and Majau for their support during its preparation. Your patience and encouragement as I stayed away for long, either in class throughout the weekends, or in the field was really touching.

ACKNOWLEDGEMENT

A major research project like this is never the work of anyone alone. The contributions of many different people, in their different ways, have made this possible.

First, I would like to thank God for the wisdom and perseverance that HE has bestowed upon me during this research project, and indeed, throughout my life.

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I wish to thank the respondents who participated in this study. I thank my parents for supporting me throughout all my studies from nursery school to university level. I can't express my gratitude in words for my family. You have been a source of strength.

God bless you mightly.

ABSTRACT

The purpose of this study was to assess the effect of investment strategies on the financial performance of collective investment schemes in Kenya. The research questions therefore were; what are the preferred investment strategies by collective investment schemes and what is the effect of investment strategies on the financial performance of collective investment schemes in Kenya?

The research design was descriptive survey study in nature since it focused on all collective investment schemes in Kenya. The population of the study was all the collective investment schemes in Kenya. This implied that the total population of this study is 16 investment schemes firms. The study used both primary and secondary data from the financial statements of the investments firms. The selected period was 5 years. The researcher used frequencies, averages and percentages in this study. The researcher used Statistical Package for Social Sciences (SPSS) to generate the descriptive statistics and also to generate inferential results. Regression analysis was used to demonstrate the relationship between the investment strategies and the profitability of the collective investment schemes.

The findings reveal that collective investment schemes in Kenya had adopted two types of strategy which are passive and active. However the study findings revealed that these strategies were further categorized into five categories which include aggressive, value, moderate risk, conservative and high risk aversion strategies. The findings also revealed that there was a positive and significant relationship between investment strategy and profitability and return on assets.

The study recommended that the collective investment schemes to pursue passive strategy because it yields superior profitability than active strategy, that the firms should pursue passive strategy as it yields superior returns on assets compared to active strategy, It was also recommended that the governance structures need to be put in place so as to enhance returns of the stock exchange and that the investment firms to adopt different forms of investments such as investment property, real estate investments, mutual funds, government securities and equity.

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LIST OF ACRONYMS

CIS.....	Collective Investment Scheme
CMA.....	Capital Market Authority
EMH.....	Efficient Markets Hypothesis
IRR.....	Internal Rate of Return
NPV.....	Net present Value
PI.....	Profitability Index
REITS.....	Real Estate Investment Trusts
SPSS.....	Statistical Package for Social Sciences
US.....	United States

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Murad (1964), defines the term investment as the purchase of any income-yielding asset, such as securities or real estate. Investment can also be defined as the addition to the value of the capital equipment which has resulted from the productive activity of the period. There is a variety of reasons why an economic agent such as a household or a firm can engage in investments. The primary reason for engaging in investment is to earn returns. Other reason for investing is to increase some ones wealth. The only way to protect savings is to invest it in products that have the ability to grow at a faster rate than that of inflation. Another reason to invest is to achieve the longer term financial goals such as retiring from work to live a life of leisure. Or it can be investing the money to provide a certain level of income during retirement

1.1.1 Concept of Investment Strategies

Jones (2009) defines investment strategy as a set of rules or procedures that guide an investor's selection of an investment portfolio. The strategy is designed around the investor's risk-return trade off. A well planned investment strategy is essential before having any investment decisions. Investment strategies are ways by which an investor can acquire the expected return, given a specific risk tolerance level. Investment strategies are adopted at organizational, industry and market level and serve as a guide for entering and selecting investment portfolios (Fama & French, 1992).

There are two main investment strategies; passive investments strategy and active investment strategy. Ferri (2009) states that passive strategies are the strategies that are used to minimize transaction costs. It entails tracking of market without attempting to anticipate its evolution. An assumption is made that financial markets are perfectly efficient and they immediately integrate all information that is needed to influence prices of investments. One of the effective passive investments strategy is the buy-and-hold investing. The main advantage of the passive investment strategy it has lower operating costs (Jones, 2009).

Schoenfeld and Steven (2004) states that active strategies are strategies that are all about achieving returns that are superior to the financial markets .The strategies attempt to maximize

returns like market timing whereby an investor enters the market on the lows and sells on the highs. This could as well mean buying investment instruments when they are cheap and selling them off when their prices appreciate. This strategy attempts to outperform the market with a goal to beat a particular benchmark. The active investment strategy involves the investor actively monitoring the activity of the investments and exploits any profitable condition available.

1.1.2 Financial Performance of Investment Firms

Different organizations measure performance differently. It is therefore important to understand the term performance so as to know how to apply given a certain context. Guest et al (2003) defined performance as outcomes, end results and achievements (negative or positive) arising out of organizational activities.

Collective investment firms mostly gauge their performance from two perspectives; from the customer perspective and from the firm's perspective. The customer perspective entails the rates of returns that the customers are entitled on the principal invested. The firm's perspective entails factoring in the returns paid to customers. The balance is then adjusted from the administrative costs such as salaries and depreciation. The final figure may be adjusted for interest expenses and taxes in order to give the profit after interest and tax.

Rudolph (2011) conducted a study on the U.S. Insurance Company Investment Strategies in an Economic Downturn. The author observed that nearly all insurance companies reported having well-defined investment policy statements (IPS), approved by their board, which are flexibly written and have evolved over time. Only 3% reported having no IPS. In addition, the author found that most insurance firms used a conservative investment strategy, had limited leverage, Focused on core offerings and depended on recurring premiums.

The empirical study of Su and Vo (2010) found that combined effect of corporate strategy and capital structure explains firms' performance very well. This implies that there are other intervening factors, other than investment strategies, that affect performance. On the other hand, Singhanian and Seth (2010) in their empirical study for listed companies in Bombay Stock Exchange found that there exists a negative association between debt ratio and company growth, but there exists a positive association between debt ratio and company size.

1.1.3 Collective Investment Schemes

In Kenya, capital markets offer an array of investment products in the form of shares, bonds and unit trusts (CMA, 2009). Investors' choice depends on financial goals, time frame, amount of capital available, potential risk and returns. CMA (2010) records that the number of unit trust licensees in Kenya had grown from virtually zero in 2001 to 11 in 2008 with a sum of KShs. 20 billion indicating increased acceptance and popularity in recent years. Irungu (2008) attributed the slow growth of investment in unit trusts in Kenya to high upfront fees and inadequate disclosures.

However, CMA (2010) notes that as the capital markets become sophisticated and more volatile, unit trusts have become safe havens for less, sophisticated and less capitalized, conservative individuals in the market place. CMA (2011) note that there are 16 CMA approved CIS in Kenya offering 37 different open-ended type of unit trust funds in Kenya. Irungu (2008) further points out that CIS take the careful position; risk aversion, since the current funds in Kenya are the open-ended type that basically allows members to enter and exit as they desire hence the need for liquidity. The list of approved CIS is presented at the appendix.

1.2 Statement of the Problem

Investments are an important factor in the profitability of the investment firms. The investment performance of the fund assets is the most important factor in determining whether the fund will be able to deliver on the retirement benefits...or whether there will be a sufficient amount accumulated...for an adequate replacement of income. Investment strategy is the way a manager goes about analyzing, buying, and selling stocks. CMA (2011) records that the number of unit trust licensees in Kenya had grown from virtually zero in 2001 to 11 in 2008 and to 16 as at 2011. Despite the growth in number, the collective schemes have witnessed slow growth (Kogi, 2003; Irungu, 2008). This is perhaps due to the type of investments, investment strategies and the resultant poor performance that they achieve.

Empirical studies on the area of investment strategy and return concentrate on market timing ability and its role in delivering superior returns. Christensen (2005) reviewed the Danish mutual fund performance by focusing on selectivity, market timing and persistence. Chen and Liang (2005) attempted to analyze whether market timing hedge funds are successful in timing

the market. Treynor and Mazuy (1966) attempted to analyze whether mutual funds can outguess the market. Merton and Henriksson (1981) reviewed statistical procedures for evaluating forecasting skills and their role in market timing and investment performance. The studies by Christensen (2005), Chen and Liang (2005), Treynor and Mazuy (1966) and Merton and Henriksson (1981) have mixed conclusions on the ability of market timing to deliver superior or above market returns. While Chen and Liang (2005) find evidence of a positive relationship between market timing and returns, Christensen (2005) does not. This implies that globally, this area of study is riddled by inconclusiveness.

Locally, Wambui (2010) investigated the existence of real estate investment trusts (REITS) needs by institutional investors at the NSE and concluded that investors needed an avenue of investing in real estate without incurring the challenges associated with acquiring real estate. Nyale (2010) investigated the relationship between leverage and investment decisions for companies quoted at the NSE. Kogi (2003) conducted a study on the future of collective investment schemes in Kenya and concluded that collective investments had experienced slow growth. This is perhaps due to the type of investments and investment strategies that they adopt. However, the above local studies (Wambui, 2010; Nyale, 2010, Kogi, 2003) were inconclusive and failed to address the effect of investment strategies on the performance of investment firms. The closest study to the current one was by Mulindu (2007) who analyzed the impact of investment strategies on the performance of managed funds in Kenya. She took a case study of Fedha Management Limited and concluded that the poor performance of the managed funds could be attributed to the inconsistent use of strategies by managers and the emotional approach to investment management. The author asserted that pressure from emotional clients made investment managers change their investment strategies frequently which led to losses. There has not been an attempt to assess the effect of investment strategies and profitability on the investment firms in Kenya since Mulindu (2007). Therefore, the researcher does not know of any other study that has been conducted on this area. This study research question there is; what is the effect of investment strategies on the performance of investment firms in Kenya?

1.3 Objectives of the Study

1.3.1 Main Objective of the Study

The purpose of the study was to investigate the effect of investment strategies on the financial performance of collective investment schemes in Kenya.

1.3.2 Specific Objectives of the Study

- 1 To identify the preferred investment strategies by collective investment schemes in Kenya
- 2 To investigate the effect of investment strategies on the financial performance of collective investment schemes in Kenya.

1.4 Significance of the Study

The study results may inform policy. The study will be useful to the government of Kenya in their endeavor to regulate the investment industry most particularly on profitability, liquidity and solvency of the industry. The industry regulating body, the CMA and IRA, will also find the results of this study very invaluable, as it will be able to ascertain investments strategies that enhance financial performance of an individual firm and as so determine whether such practices adopted in the industry conform to the guidelines provided for the industry by the government.

The study results may inform practice. Investment managers of collective investment schemes may use the findings to decide whether to adopt passive or active strategies.

The study results may add value to academic theory building. Future researchers can use the study to enrich their research and it will form a basis for further research. The students and academics institutions will use this study as a basis for discussions on Investment strategies adopted by the Kenyan investment firms and how the strategies affect their financial performance. The study will add to the existing knowledge of the investments and profitability.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

The chapter explores the literature that focuses on the area of investment strategies and the relationship of such strategies to the profitability of the investment firms. The chapter commences by defining what investment strategies are. It then dwells on the theories of investments after which it discussed the concept of effects of the strategies on financial performance of investment firms.

2.1: Theoretical Review

Investment strategy is set of rules and procedures that guide an investor's selection of an investment portfolio. A firm's investment decision is the decision to invest its current funds most efficiently in the long-term assets in anticipation of expected benefits over a series of years. The long-term assets are those that affect the firm's operations beyond one-year period (Jones,2009). Pandey (2005) gives the features of investment decisions as; the exchange of current funds for future benefits, the funds are invested in long-term assets and the future benefits will occur to the firm over a series of years. The firm's investment decision affects its value in that the firm's value will increase if the investment decisions are profitable and add value to the shareholder's wealth.

2.1.1 Efficient Market Hypothesis Theory

The efficient markets hypothesis (EMH), popularly known as the Random Walk Theory, is the proposition that current stock prices fully reflect available information about the value of the firm, and there is no way to earn excess profits, (more than the market overall), by using this information. It deals with one of the most fundamental and exciting issues in finance – why prices change in security markets and how those changes take place. It has very important implications for investors as well as for financial managers (Jensen, 1968).

The first time the term "efficient market" was in a 1965 paper by E.F. Fama who said that in an efficient market, on the average, competition will cause the full effects of new information on intrinsic values to be reflected instantaneously in actual prices. Many investors try to identify

securities that are undervalued, and are expected to increase in value in the future, and particularly those that will increase more than others (Malkiel, 1999; Fama, 1998).

Many investors, including investment managers, believe that they can select securities that will outperform the market. They use a variety of forecasting and valuation techniques to aid them in their investment decisions. Obviously, any edge that an investor possesses can be translated into substantial profits (Fama, 1998).

Arguably, no other theory in economics or finance generates more passionate discussion between its challengers and proponents. For example, noted Harvard financial economist Michael Jensen writes that there is no other proposition in economics which has more solid empirical evidence supporting it than the Efficient Market Hypothesis, while investment maven Peter Lynch claims that efficient markets is a bunch of junk, crazy stuff (Fortune, April 1995).

The efficient markets hypothesis (EMH) suggests that profiting from predicting price movements is very difficult and unlikely. The main engine behind price changes is the arrival of new information. A market is said to be efficient if prices adjust quickly and, on average, without bias, to new information. As a result, the current prices of securities reflect all available information at any given point in time. Consequently, there is no reason to believe that prices are too high or too low. Security prices adjust before an investor has time to trade on and profit from a new piece of information (Jensen, 1968; Malkiel, 1995; Sharpe, 1966; Treynor, 1965)

The key reason for the existence of an efficient market is the intense competition among investors to profit from any new information. The ability to identify over- and underpriced stocks is very valuable, it would allow investors to buy some stocks for less than their true value and sell others for more than they were worth. Consequently, many people spend a significant amount of time and resources in an effort to detect mispriced stocks. Naturally, as more and more analysts compete against each other in their effort to take advantage of over- and undervalued securities, the likelihood of being able to find and exploit such mispriced securities becomes smaller and smaller. In equilibrium, only a relatively small number of analysts will be able to profit from the detection of mispriced securities, mostly by chance. For the vast majority of investors, the information analysis payoff would likely not outweigh the transaction costs (Sharpe, 1966; Treynor, 1965).

2.1.2 Three Versions of the Efficient Markets Hypothesis

The efficient markets hypothesis predicts that market prices should incorporate all available information at any point in time. There are, however, different kinds of information that influence security values. Consequently, financial researchers such as Jensen, (1968); Malkiel, (1995) distinguish among three versions of the Efficient Markets Hypothesis, depending on what is meant by the term all available information.

2.1.3 Weak Form Efficiency

The weak form of the efficient markets hypothesis asserts that the current price fully incorporates information contained in the past history of prices only. That is, nobody can detect mis-priced securities and beat the market by analyzing past prices. The weak form of the hypothesis got its name for a reason because security prices are arguably the most public as well as the most easily available pieces of information. Thus, one should not be able to profit from using something that everybody else knows. On the other hand, many financial analysts attempt to generate profits by studying exactly what this hypothesis asserts is of no value - past stock price series and trading volume data. This technique is called technical analysis (Malkiel, 1999; Fama, 1998).

The empirical evidence for this form of market efficiency, and therefore against the value of technical analysis, is pretty strong and quite consistent (Treyner, 1965). After taking into account transaction costs of analyzing and of trading securities it is very difficult to make money on publicly available information such as the past sequence of stock prices.

2.1.4 Semi-strong Form Efficiency

The semi-strong-form of market efficiency hypothesis suggests that the current price fully incorporates all publicly available information. Public information includes not only past prices, but also data reported in a company's financial statements i.e. annual reports, income statements, filings for the Security and Exchange Commission, earnings and dividend announcements, announced merger plans, the financial situation of company's competitors, expectations regarding macroeconomic factors (Elton, Gruber & Blake, 1995).

The public information does not even have to be of a strictly financial nature. The assertion behind semi-strong market efficiency is still that one should not be able to profit using information that is public. Nevertheless, this assumption is far stronger than that of weak-form

efficiency. Financial researchers have found empirical evidence that is overwhelming consistent with the semi-strong form of the EMH (Elton, Gruber & Blake, 1995).

2.1.5 Strong Form Efficiency

The strong form of market efficiency hypothesis states that the current price fully incorporates all existing information, both public and private, sometimes called inside information. The main difference between the semi-strong and strong efficiency hypotheses is that in the latter case, nobody should be able to systematically generate profits even if trading on information not publicly known at the time. In other words, the strong form of EMH states that a company's management are not be able to systematically gain from inside information by buying company's shares ten minutes after they decided, but did not publicly announce to pursue what they perceive to be a very profitable acquisition (Malkiel, 1995).

In addition, the members of the company's research department are not able to profit from the information about the new revolutionary discovery they completed half an hour ago. The rationale for strong-form market efficiency is that the market anticipates, in an unbiased manner, future developments and therefore the stock price may have incorporated the information and evaluated in a much more objective and informative way than the insiders. Not surprisingly, though, empirical research in finance has found evidence that is inconsistent with the strong form of the EMH (Malkiel, 1999; Fama, 1991, Fama, 1998).

2.1.6 Investment Strategies

Jones, (2009) defines investment strategy as a set of rules or procedures that guide an investor's selection of an investment portfolio. The strategy is designed around the investor's risk-return trade off. A well planned investment strategy is essential before having any investment decisions. Investment strategies are ways by which an investor can acquire the expected return, given a specific risk tolerance level. Investment strategies are adopted at organizational, industry and market level and serve as a guide for entering and selecting investment portfolios (Fama & French, 1992). There are two main investment strategies; passive investments strategy and active investment strategy.

Ferri, (2009) states that passive strategies are the strategies that are used to minimize transaction costs. It entails tracking of market without attempting to anticipate its evolution. An assumption

is made that financial markets are perfectly efficient and they immediately integrate all information that is needed to influence prices of investments.

One of the effective passive investments strategy is the buy-and-hold investing. Buy and hold strategy is a long-term investments strategy whereby an investor holds an investment for the long haul in the hope that in the long run the investment will give a better rate of return. This strategy is beneficial for small investors. In a situation where the investment is a real estate, the holding period could span into a mortgage. The main advantage of the passive investment strategy it has lower operating costs (Jones, 2009).

Schoenfeld and Steven (2004) states that active strategies are strategies that are all about achieving returns that are superior to the financial markets .The strategies attempt to maximize returns like market timing whereby an investor enters the market on the lows and sells on the highs. This could as well mean buying investment instruments when they are cheap and selling them off when their prices appreciates. This strategy attempts to outperform the market with a goal to beat a particular benchmark. The active investment strategy involves the investor actively monitoring the activity of the investments and exploits any profitable condition available.

The active investment methods may include fundamental analysis, technical analysis, quantities analysis and analysis of the environment. Active investment management involves developing strategies to take advantage of temporary market inefficiencies. Most investors, who undertake this strategy, are looking for short-term profits. This strategy is beneficial for big-time investors. The active investment may be advantageous in its possibility that the managers of the portfolio may able to outperform the index due to their superior skills. However, it may disadvantageous it is more costly because of the high fees and operating expenses resulting from regular monitoring (Ferri, 2009).

2.1.6.1 Types of Investment Strategies

2.1.6.2 Aggressive Investment Strategy

These investors focus on high return investments in the short to medium term. To achieve these high returns, they are willing to take higher risk. They aim at outperforming the market with their investment portfolio through quick adjustments (Schoenfeld and Steven ,2004).

2.1.6.3 Value Investment Strategy

Value investors hope to get lucky with a surprise dark horse investment. They invest after detailed research and analysis of the company and the industry. Their assumption is that the market is yet to realize the potential of the stock and once it does, the price will go up significantly. These investors sometimes hit upon a gold mine stock and make a huge profit. This kind of investing should not be confused with rash investments where the investor has no structured plan or strategy and acts on the basis of nothing more than hot tips from dubious sources (Jones, 2009).

2.1.6.4 Moderate Risk Investment Strategy

In moderate risk investing, the investor attempts to minimize the risk in their portfolio by adding a few stable stocks. These balance out the high risk stocks in their portfolio and keep their investment from being wiped out in case the markets go into a nosedive. Moderate investors tend to make lower profits but get more stability in the portfolio. They are somewhat protected against the volatility of the market (Ferri, 2009).

2.1.6.5 Conservative Investment Strategy

This kind of investing is carried out by investors who seek a consistent and dependable income rather than huge profits that come through higher risks. Many retirees adopt a conservative investment approach to make sure they do not lose their savings through rash investment decisions, yet get decent returns to pay the bills. Blue chip stocks are the best option for these investors (Fama & French, 1992).

2.1.6.6 High Risk Averse Investment Strategy

Even in market conditions showing definite bull tendencies, highly risk averse investors hesitate to make purchases. They hold back because of fear of losing money and thus fail to make the most of the stock market movements. This highly cautious approach is not suited to stock market investing. Though such investors seldom lose money, they don't make a lot of profit either (Ferri, 2009).

2.1.7 Modern Portfolio Theory of Stock Selection

Asset allocation, diversification and rebalancing are all part of a sound investment strategy that is built around the time-tested economic concepts of Modern Portfolio Theory. By using these financial concepts, an investor gets an easy-to-follow investment plan tailored to his/her needs. Investors who invest their hard-earned money naturally want to minimize their risks, while maximizing their potential returns. This is the basis of Modern Portfolio Theory (MPT), the foundation of investment strategies. Developed by Nobel Laureate Harry Markowitz, and refined by other noted economists over the years, MPT suggests that you can limit the volatility in your portfolio, while improving its performance, by spreading the risk among different types of securities that don't always behave the same way (Markowitz, 1952).

It is a principle of investing that the higher the risk, the higher the potential return and conversely, the lower the risk, the lower the return. According to MPT, a portfolio (a combination of individual investments) exhibits risk and return characteristics based on its composition and the way those components correlate with each other. For each level of risk, there is an "optimal" asset allocation that is designed to produce the best balance of risk versus return. An optimal portfolio will provide neither the highest returns, nor the lowest risk of all possible portfolio combinations – it will attempt to balance the lowest risk for a given level of return and the greatest return for an acceptable level of risk. This meeting point of each level of risk and reward, where the optimal portfolios reside, is called the "Efficient Frontier."

2.1.8 Information Signaling Hypothesis/Theory

The concept of signaling was first studied in the context of job and product markets by Akerlof and Arrow and was developed into signal equilibrium theory by Spence (1973), which says a good firm can distinguish itself from a bad firm by sending a credible signal about its quality to capital markets. The signal will be credible only if the bad firm is unable to mimic the good firm by sending the same signal. If the cost of the signal is higher for the bad type than that of the good type firm, the bad type may not find it worthwhile to mimic, and so the signal could be credible. Ross (1977) shows how debt could be used as a costly signal to separate the good from the bad firms. Under the asymmetric information between management and investors, signals from firms are crucial to obtain financial resources. Ross assumes that managers (the insiders)

know the true distribution of firm returns, but investors do not. Signaling of higher debt by managers then suggests an optimistic future and high quality firms would use more debt while low quality firms have lower debt levels. In this way, a good firm can separate itself by attracting scrutiny while the bad firm will not mimic because the bad firm will not want to be discovered.

2.2 Empirical Review

Rudolph (2011) conducted a study on the U.S. Insurance Company Investment Strategies in an Economic Downturn. The author observed that nearly all insurance companies reported having well-defined investment policy statements (IPS), approved by their board, which are flexibly written and have evolved over time. Only 3% reported having no IPS. These policy documents guided management and staff through the crisis, providing stability and enabling better performance during this period. This was true for companies of all sizes and types, although each firm had a unique experience. In addition, the author found that most insurance firms used a conservative investment strategy, had limited leverage, Focused on core offerings and depended on recurring premiums.

Sehhat and Rad (2011) conducted a study on matching investment strategies for insurance firms and concluded that one of the difficulties of insurance company's investment is selecting and choosing proper investment strategies for paying futures liabilities. The authors noted that indeed, the most concern of insurance manager is the capacity of paying liabilities, even more than profitability and return on investment.

Mulindu (2007) analyzed the impact of investment strategies on the performance of managed funds in Kenya. She took a case study of Fedha Management Limited and concluded that the poor performance of the managed funds could be attributed to the inconsistent use of strategies by managers and the emotional approach to investment management. The author asserted that pressure from emotional clients made investment managers change their investment strategies frequently which led to losses.

Mutswenje (2009) conducted a survey of the factors influencing investment decisions by taking the case of individual investors at the NSE. The author concluded that personal factors such as gender, income status, level of education, level of experience with stock market, the characteristics of the securities, and the investor needs influenced the investment decision.

However, the study did not address the type of investment decisions adopted by investment firms and insurance firms.

Wambui (2010) investigated the existence of real estate investment trusts (REITS) needs by institutional investors at the NSE and concluded that investors needed an avenue of investing in real estate without incurring the challenges associated with acquiring real estate.

Nyale (2010) investigated the relationship between leverage and investment decisions for companies quoted at the NSE. The author concluded that leverage influenced the investment decisions of quoted companies with high leveraged companies requiring a higher rate of return for their investments. However, restrictive covenants were also factored in when making investment decisions.

Kogi (2003) conducted a study on the future of collective investment schemes in Kenya and concluded that collective investments had experienced slow growth. Kogi (2003) made several observations. First, the slow growth was perhaps due to the type of investments and investment strategies that they adopted. In addition, the author cited low public awareness, low investor education, lack of public trust and low returns as challenges facing the growth of collective investment schemes.

The work by Modigliani and Miller (1958), who advocated the irrelevance of investment and financing decisions, gave rise to broad interests in topics on funding policy or capital structure. Some aspects switch from independence to interdependence between investment and financing decisions. For example, Brennan and Schwartz (1984), Mellon and Parsons (1992), Mauer and Triantis (1994), Mauer and Ott (2000), Hennessy and Whited (2005), and Titman and Tsyplakov (2007) all advocate that investment decisions are dependent on financial decisions. Some of them distinguish funding policy between external (debt) and internal (equity) sources (Hennessy and Whited; Titman and Tsyplakov; Strebulaev, 2006).

Among these scholars who focus on interdependence between investment and financial decisions, only Titman and Tsyplakov lays emphasis on firms' investment flexibility, which allows a firm to defer its investment action until the optimal entry time. The study of Azofra and Miguel (1990), who adopt a simultaneous system of equations as the estimation procedure, obtains a direct relationship between investment and debt. The empirical study of Su and Vo

(2010) found that combined effect of corporate strategy and capital structure explains firms' performance very well.

2.3: Collective Investment Schemes and Types of Investments

Collective investment schemes usually invest in several types of investment. This is done in a bid to caution against low performance of one security. In this study, the researcher will analyze the type of investments in each of the investment firms under study to establish how much investment have been done by the firm and compare that, with the profitability of the firm. This will help establish if the investment strategies play any role on the profitability of the investment firms in Kenya.

A number of investments criteria are in practice. They may be grouped in the following two categories. The first category is Discounted Cash flow Criteria which consists of Net present Value (NPV), Internal rate of Return (IRR) and Profitability Index (PI) .The second category is Non-Discounted Cash Flow Criteria which consists of Payback Period, Discounted Payback Period and Accounting Rate of Return.

Net Present Value Method is a classic economic method of evaluating the investment proposals. It recognizes the time value of money. It correctly postulates that cash flow arising at different time periods differ in value and are comparable only when their equivalents present values is found out. The internal rate of Return method takes into account the magnitude of timing cash flows. The Internal rate of Return is the rate that equates the investments outlays with the present value of cash inflow received after one period. Profitability Index is the ratio of the present value of cash inflows at the required rate of return, to the initial cash outflow of the investment (Pandey, 2005)

The payback method is one of the most popular and widely recognized traditional methods of evaluating investments because of its simplicity. Pay back method is the method that uses the number of years required to recover the original cash outlay invested in a project. The Discounted payback method is an enhanced version of the Payback method that takes into account discounting of the cash flows then calculates the payback. The Discounted payback Period is the number of periods taken in recovering the investment outlay on the present value basis. Finally, the Accounting rate of Return method also known as return on investment uses

accounting information as revealed by financial statements, to measure profitability of an investment. It is the ratio of the average after tax profit divided by the average investment (Pandey, 2005).

Sornette (2003) indicates that there are several forms of Investments that include investment property, (Buildings), real estate investments, mutual funds, government securities (treasury bills and bonds), deposits with financial institutions (fixed deposits and On-call deposits), investment in associates, investments in subsidiaries and investments in stocks (Equity). Shefrin (2006) argues that overall, there are three different kinds of investments. These include stocks, bonds and Cash. The different types of Investments can also be put in two categories of risk tolerance of either high risk or low risk depending on how risky it is to invest in such investments.

Sornette (2003) further explains that when an investor buys stocks (Shares) in a company, they buy ownership in the company. There are two ways to make money using stock which are; capital gains and dividends from the company. Bonds are debt investments and they represent a loan that investor makes to an institutions. It could be corporate bond or a government bond in exchange for interest which become due during a specific term plus the repayment of the principal amount when the bond becomes due. An investor makes money from a bond through capital gains and Interests.

Mutual Funds are a popular way to invest in securities because they can offer built-in diversification and professional management. Like investing in any security, investing in mutual fund also carry a certain amount of risk. Real estate investments are investments in mortgages and real estate. It is important for an organization to have a mix in the investments to caution against bad economic times for a certain type of investment (Sornette, 2003).

Pandey (2008) says that there are many ways to classify investments. Some of the classifications are expansion of existing business, expansion of new business, replacement and modernization of equipments. According to Niehaus and Harrington (2003) insurance companies usually invest in mortgages and real estate, cash and short term, corporate bonds and government bonds and Common and preferred stocks.

2.4 Chapter Summary

CFC Stanbic Bank Limited (2011) argues that the main objective of collective investments is to pool small amounts of money from many retail investors for large projects like providing cost effective access to a wide variety of local and international shares/equities, bonds, and money market instruments such as fixed deposits, treasury bills and call accounts and to minimize the effects of different forms of risks to acceptable levels. Wambui (2010) investigated the existence of real estate investment trusts (REITS) needs by institutional investors at the NSE and concluded that investors needed an avenue of investing in real estate without incurring the challenges associated with acquiring real estate. Nyale (2010) investigated the relationship between leverage and investment decisions for companies quoted at the NSE. Kogi (2003) conducted a study on the future of collective investment schemes in Kenya and concluded that collective investments had experienced slow growth. This is perhaps due to the type of investments and investment strategies that they adopt. However, the above local studies (Wambui, 2010; Nyale, 2010, Kogi, 2003) were inconclusive and failed to address the effect of investment strategies on the performance of investment firms. Global studies are also riddled with inconclusiveness.

The closest study to the current one was by Mulindu (2007) who analyzed the impact of investment strategies on the performance of managed funds in Kenya. She took a case study of Fedha Management Limited and concluded that the poor performance of the managed funds could be attributed to the inconsistent use of strategies by managers and the emotional approach to investment management. The author asserted that pressure from emotional clients made investment managers change their investment strategies frequently which led to losses. There has not been an attempt to assess the effect of investment strategies and profitability on the investment firms in Kenya since Mulindu (2007). Therefore, the researcher research gaps stems from i) inconclusiveness of global studies (ii) inadequacy of local studies (iii) case study methodology used by Mulindu (2007) was inadequate.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1. Introduction

This chapter discussed the type of research design, population, target population, sampling frame, sample, sample size, sampling technique, instruments to be used, pilot test and data analysis.

3.2: Research design

Research design refers to how data collection and analysis are structured in order to meet the research objectives through empirical evidence economically (Chandran, 2004; Cooper and Schindler, 2006).

The current study took a descriptive survey design. The research is descriptive since it attempted to discover the status quo, that is, to report the way things are. A survey research design is adopted when one wants to gather data from more than one organization (Sekaran 2006; Cooper and Schindler, 2006).

A descriptive survey design is appropriate for this study since the study intends to collect data from several organizations.

3.3: Population

A population refers to an entire group of individuals, events or objects having a common observable characteristic (Mugenda and Mugenda, 2003). The population of the study was all the investment firms in Kenya. Specifically, the investment industry composed of 16 investment schemes. This implied that the total population of this study was 16 firms.

3.4: Sample

A sampling frame for this study is the list of collective investment firms given by Capital markets authority of Kenya as at December 2011. A census methodology was carried out for this study since the number of collective investment firms was few. The list is provided at the appendix.

3.5: Data Collection Tools and Methods

The preferred data collection instrument is a questionnaire. A questionnaire is a list of research or survey questions asked to respondents and designed to extract specific information. Each item in the questionnaire is used to address a specific objective, research question or hypothesis study. A questionnaire can contain open or closed questions or it can be a mix of both closed and open questions (Cooper and Schindler, 2007).

The questionnaire had three main parts; Demographic information, the preferred investment strategies by the investment firms and the effects of investment strategies on the financial performance of investment firms.

Primary data collected through a questionnaire was used to achieve the objectives. Secondary data was also used.

3.5.1 Data Validity and Reliability

The reliability of the data was tested using cronbach alpha statistic. A cronbach statistic of more than 0.7 implied that the data collection instrument is reliable (Cronbach, 1951). The validity of the questionnaire was tested by subjecting it to peers and experts.

3.6: Data Analysis

The researcher used frequencies, averages and percentages in this study. The researcher used Statistical Package for social Sciences (SPSS) to do the data analysis Regression analysis was used to demonstrate the relationship between the investment strategies and the profitability of the investments firms in Kenya. According to Mugenda and Mugenda (2003), the regression technique is used to analyze the degree of relationship between two variables.

3.6.1 Conceptual Model:

The conceptual model was as follows;

$$\text{Performance} = f(\text{Investments strategy})$$

Performance is a function of investment strategy.

3.6.2 Empirical Model:

Performance was measured by 3 indicators; profitability before tax (PBT) and Return on assets.

Investment strategy was demonstrated by a dummy variable: Active Strategies were allocated 1 and 2 for passive strategies.

The empirical model was as follows;

$$Profitability = a + b_1 Investment Strategy + e$$

$$ROA = a + b_1 Investment Strategy + e$$

Where;

Profitability = profit before tax of an investment scheme

ROA = Return on assets of a collective investment schemes

a' = constant

b1 = regression coefficients

e = error terms

Expectations

Active investment strategies (dummy variable 1) are negatively related to profitability, ROA and market share

Passive investment strategies (dummy variable 2) are positively related to profitability, ROA and market share

The findings were interpreted though looking at the sign of the regression coefficients. The significance of the choice of investment strategy was checked through p values, where a p value of less than 0.05 indicated that the choice of investment strategy plays a significant role on performance.

The basis of the model is empirical evidence that links investment strategy to financial performance. For example Chen and Liang (2005) who investigated market timing strategy and performance and concluded that market timing strategy is an active strategy that influences financial performance therefore the assumption of the model used in this study is based on the findings of Chen and Liang. Other studies that inform the basis of this model include Christensen(2005) and Mulindu 2007.

The dummy was sufficient because it was not assigned arbitrary values; it was arrived at after rigorous analysis of statement that presented either an active or passive strategy. A CIS whose mean score for active strategy is higher than its passive score was labeled as active and was assigned a dummy variable of 1. A CIS whose mean score for passive strategy was higher than its active score was labeled as passive and was assigned a dummy variable of 2.

3.6.3 Operationalization of the Questionnaire.

The question 8 of the questionnaire has a set of set of questions that attempted to measure the type of investment strategy. Statement 1 to statement 6 represents active strategies (Aggressive Investment strategy, Value Investment strategy Moderate Risk Investment strategy in that order).

Statement 7 to 10 represents passive strategies (conservative and highly risk adverse strategy). Mean scores of the two groups were calculated. A CIS whose mean score for active strategy is higher than its passive score was labeled as active and was assigned a dummy variable of 1. A CIS whose mean score for passive strategy was higher than its active score was labeled as passive and was assigned a dummy variable of 2.

This operationalization is based on the assumption that a CIS pursue more than one type of investment strategies owing to the diverse requirements of its clientele.

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION OF FINDINGS

4.1 Introduction

The chapter dealt with the presentation of the findings. The descriptive statistics were presented first followed by the trend analysis. The analytical model results were presented last. A discussion of the results was also presented and the findings were compared with empirical literature.

The respondents were asked to state how long had their firm been in existence. A majority (62.5%) indicated that their firms had been in existence for a period of between 5 to 10 years while 37.5% said that their firms had been in existence for over 10 years. The results are presented in table 4.1.

Table 4. 1: Period of existence

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Btw 5-10 yrs	10	62.5	62.5	62.5
Over 10 yrs	6	37.5	37.5	100.0
Total	16	100.0	100.0	

4.2 Types of Investments

The study sought to identify the type of investments that the firm undertakes. The respondents were asked to indicate the value of investments that the firm had been undertaking. The results are presented in table 4.2. Results revealed that local stocks had a mean score of ksh 6183.09 millions for firms pursuing an active investment strategy while those pursuing a passive investment strategy had a mean investment of local stocks worth ksh 1913.18 millions to the same asset class.

Active firms had allocated an average of ksh 1648.70 millions to international equity while passive firms had allocated a mean of ksh 417.07 millions. Active firms had allocated an average of ksh 1698.17 millions to cash equivalents while passive firms had allocated a mean of ksh 429.58 millions to the same asset class.

Results further revealed that Active firms had allocated an average of ksh 720.87 millions to bonds while passive firms had allocated a mean of ksh 2384.40 millions to the same asset class.

Results further revealed that Active firms had allocated an average of ksh 591.33 millions to real estate properties while passive firms had allocated a mean of ksh 2371.30 millions to the same asset class. Results revealed that Active firms had allocated an average of ksh 197.50 millions to futures and options while passive firms had allocated a mean of ksh 274.44 millions to the same asset class. Results revealed that Active firms had allocated an average of ksh 582.44 millions to investments in associates and subsidiaries while passive firms had allocated a mean of ksh 2134.20 millions to the same asset class.

Asset Class	Active Firms (Average)	Passive Firms (Mean)
Bonds	720.87	2384.40
Real Estate Properties	591.33	2371.30
Futures and Options	197.50	274.44
Investments in Associates and Subsidiaries	582.44	2134.20

Table 4. 2: Types of Investments in KSh millions

	Investment Strategy Classification	N	Mean	Std. Deviation	Std. Error Mean
Local stocks	Active Investment strategy firms	10	6183.09	1195.932	378.187
	Passive Investment strategy firms	6	1913.18	1106.350	451.665
International equity	Active Investment strategy firms	10	1648.70	1086.268	343.508
	Passive Investment strategy firms	6	417.07	186.651	76.200
cash equivalents	Active Investment strategy firms	10	1698.17	1118.856	353.813
	Passive Investment strategy firms	6	429.58	192.251	78.486
Bonds	Active Investment strategy firms	10	720.87	376.362	119.016
	Passive Investment strategy firms	6	2384.40	1378.844	562.911
Real estate properties	Active Investment strategy firms	10	591.33	402.707	127.347
	Passive Investment strategy firms	6	2371.30	1475.363	602.314
Futures and Options	Active Investment strategy firms	10	197.50	19.546	6.181
	Passive Investment strategy firms	6	274.44	41.256	16.843
Investment in associates and subsidiaries	Active Investment strategy firms	10	582.44	351.076	111.020
	Passive Investment strategy firms	6	2134.20	1286.207	525.092

4.2.1 Descriptive results on preferred Types of investments strategies

The study findings in table 4.3 indicate that the statement measuring the preference to an aggressive strategy “The firms focus on high risk high return investments in the short to medium term” attracted a mean score of 4.5 for active firms and 1.67 for passive firms. Results indicate that active firms had a mean score of 4.1 while passive firms had a score of 1.67 on the statement measuring preference of an aggressive strategy “The firm aims at outperforming the market with its investment portfolio through quick adjustments”.

Results indicate that active firms had a mean score of 4.20 while passive firms had a score of 2.17 on the statement measuring preference of a value strategy “The firm conducts market research and invests in undervalued stocks”.

Results indicate that active firms had a mean score of 3.70 while passive firms had a score of 2.67 on the statement measuring preference of a value strategy “The firm assumes that the market is yet to realize the potential of various stocks it has identified and once it does, the price will go up significantly”.

Results indicate that active firms had a mean score of 4.00 while passive firms had a score of 2.17 on the statement measuring preference of a moderate risk strategy “The Firm attempts to minimize the risk in their portfolio by adding a few stable stocks”.

Results indicate that active firms had a mean score of 3.80 while passive firms had a score of 2.17 on the statement measuring preference of a moderate risk strategy “The firm balances out the high risk stocks in their portfolio and keep their investment from being wiped out in case the markets go into a nosedive”. Results indicate that active firms had a mean score of 3.00 while passive firms had a score of 4.33 on the statement measuring preference of a conservative strategy “The firm seeks out a consistent and dependable income rather than huge profits that come through higher risks”.

Results indicate that active firms had a mean score of 3.10 while passive firms had a score of 4.50 on the statement measuring preference of a conservative strategy “The firm clientele is mainly composed of retirees who adopt a conservative investment approach to make sure they do not lose their savings and who prefer to invest in blue chip companies ”.

Results indicate that active firms had a mean score of 3.60 while passive firms had a score of 4.00 on the statement measuring preference of a high risk aversion “The firm hesitates to make purchases even in market conditions show definite bullish tendencies”.

Results indicate that active firms had a mean score of 2.30 while passive firms had a score of 3.33 on the statement measuring preference of a high risk aversion “The firm holds back because of fear of losing money and thus fails to make the most of the stock market movements”.

Table 4. 3: Preferred Types of investments strategies

Investment_Strategy_Classification		N	Mean	Std. Deviation	Std. Error Mean
AggressiveStrategy1	Active Investment strategy firms	10	4.50	.850	.269
	Passive Investment strategy firms	6	1.67	.516	.211
AggressiveStrategy2	Active Investment strategy firms	10	4.10	1.449	.458
	Passive Investment strategy firms	6	1.67	.516	.211
Value_strategy1	Active Investment strategy firms	10	4.20	1.033	.327
	Passive Investment strategy firms	6	2.17	.753	.307
Value_strategy2	Active Investment strategy firms	10	3.70	.823	.260
	Passive Investment strategy firms	6	2.67	1.211	.494
Moderate_risk_strategy1	Active Investment strategy firms	10	4.00	.000	.000
	Passive Investment strategy firms	6	2.17	1.472	.601
Moderate_risk_strategy2	Active Investment strategy firms	10	3.80	1.135	.359
	Passive Investment strategy firms	6	2.17	1.169	.477
Conservative_strategy1	Active Investment strategy firms	10	3.00	.816	.258
	Passive Investment strategy firms	6	4.33	.516	.211
Conservative_strategy2	Active Investment strategy firms	10	3.10	1.197	.379
	Passive Investment strategy firms	6	4.50	.837	.342
High_risk_aversion1	Active Investment strategy firms	10	3.60	.966	.306
	Passive Investment strategy firms	6	4.00	.632	.258
High_risk_Aversion2	Active Investment strategy firms	10	2.30	1.059	.335
	Passive Investment strategy firms	6	3.33	1.506	.615

4.2.2 Trend analysis for PBT and ROA

The study sought to establish the trend analysis for profits before tax and returns on assets for duration of the study. Results are presented in figure 4.1. Results indicated that the profit before tax for the year 2006 was ksh 12 636.28 millions for active firms and ksh 42694.84 millions for passive firms.

Profit before tax for the year 2007 was ksh 13 899.91 millions for active firms and ksh 46 964.32 for passive firms. The profit before tax for the year 2008 was ksh 13 499.91 millions for active firms and ksh 46 564.70 millions for passive firms. The profit before tax for the year 2009 was ksh 13 599.91 millions for active firms and ksh 46 664.32 millions for passive firms, while for the year 2010 was ksh 16 851.00 millions for active firms and ksh 56 935.31 millions for passive firms and for the year 2011 the profits before tax was ksh 17 251.00 millions for active firms and ksh 57 335.31 millions for passive firms. The average for all the years was ksh 14 623.00 millions for active firms and ksh 49 526 .40 millions for passive firms.

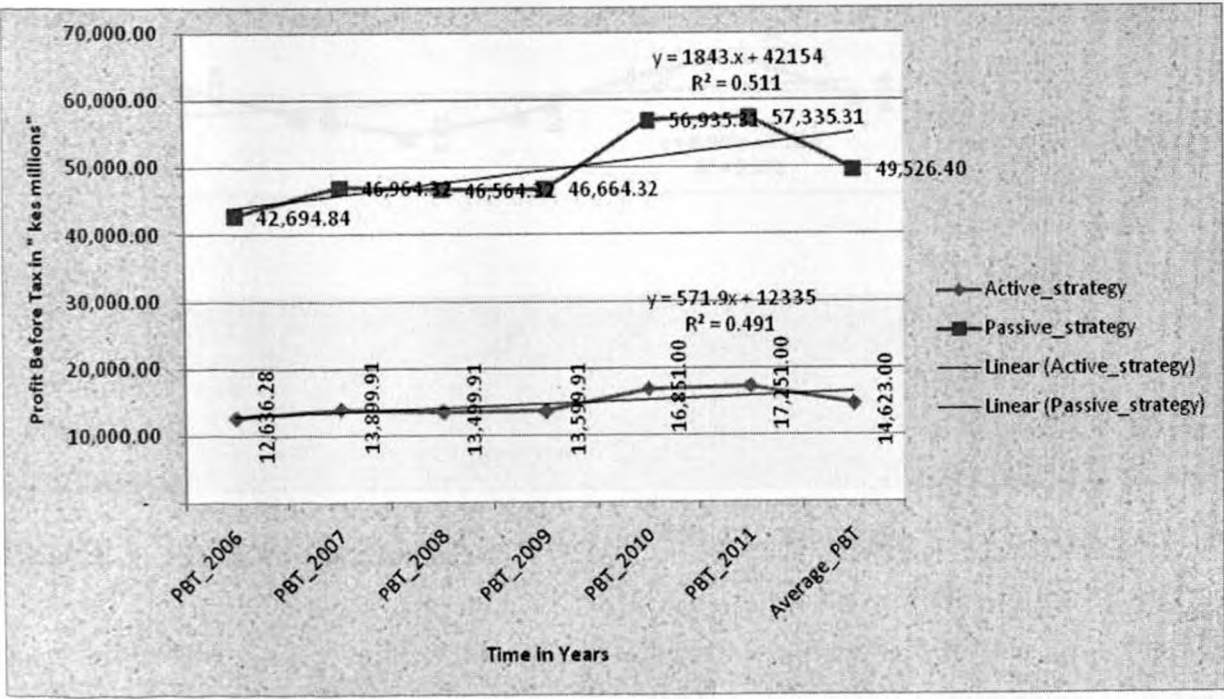


Figure 4. 1: Trend analysis for PBT

The study sought to establish the trend analysis for returns on assets for duration of the study. Results are presented in figure 4.2. Results indicated that the returns on assets for the year 2006 was 10% for active firms and 18% for passive firms. The returns on assets (ROA) for the year 2007 were 9% for active firms and 17% for passive firms. The returns on assets for the year 2008 were 8% for active firms and 16% for passive firms. The returns on assets for the year 2009 was 9% for active firms and 17% for passive firms, while for the year 2010 was 11% for active firms and 22% for passive firms and for the year 2011 the returns on assets was 12% for active firms and 23% for passive firms. The average for all the years was 10% for active firms and 19% for passive firms.

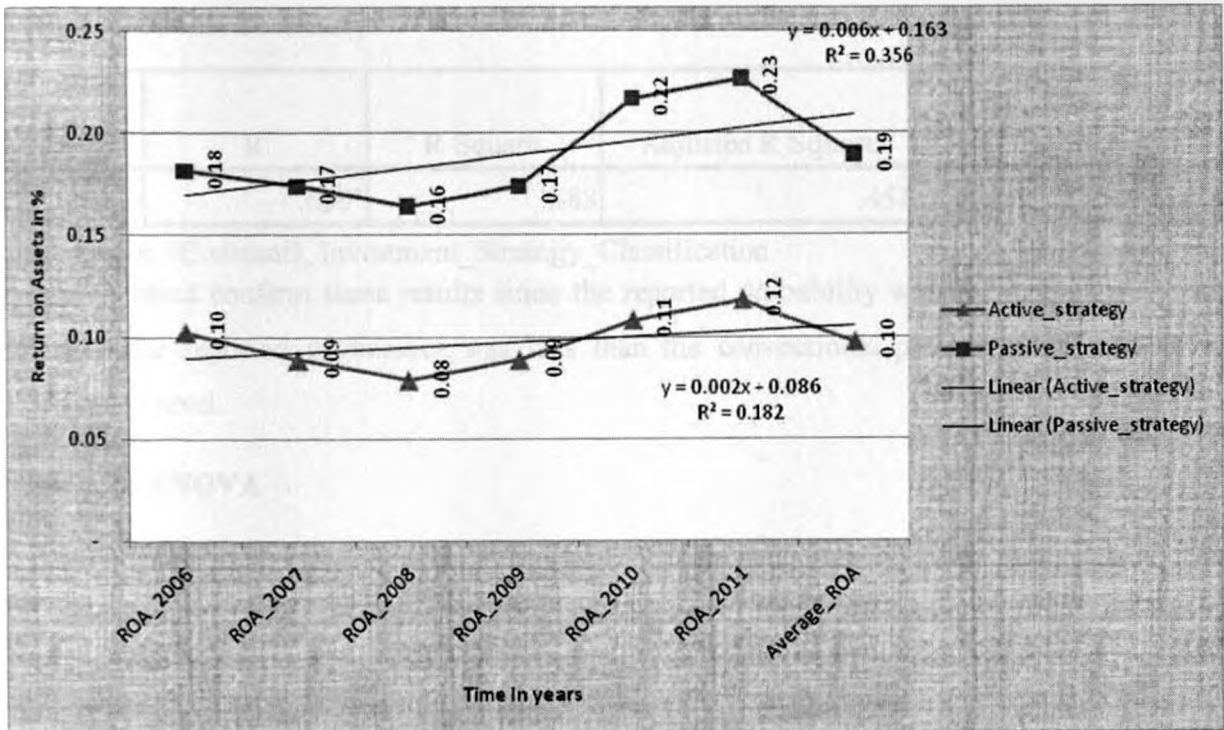


Figure 4. 2: Trend Analysis for ROA

4.3 Empirical Model Results

4.3.1 Investment Strategy and PBT

Regression analysis was conducted to empirically determine whether investment strategies were a significant determinant of profit before tax. Regression results in table 4.5 indicated the goodness of fit for the regression between investment strategy and profit before tax is satisfactory. An R squared of 0.488 indicates that 48.8% of the variance in PBT is explained by the variances in the investment strategy. The relationship between investment strategy and PBT is positive and significant ($b_1 = 34\,903.4$, p value, 0.003).

Table 4. 4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.699 ^a	.488	.451	18504.25328

a. Predictors: (Constant), Investment_Strategy_Classification

Anova statistics confirm these results since the reported probability was 0.003, for investment strategy. The reported probability was less than the conventional probability of 0.05 (5%) significance level.

Table 4. 5: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4568000000	1	4568000000	13.342	.003 ^a
	Residual	4794000000	14	3.42400000		
	Total	9362000000	15			

a. Predictors: (Constant), Investment_Strategy_Classification

b. Dependent Variable: Average_PBT

Results in table 4.7 revealed that there is a positive and significant relationship between the investment strategy and PBT. This was evidenced by a regression coefficient of 30903.402. The associated p value (sig) was 0.003.

Table 4. 6: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-20280.401	13929.496		-1.456	.167
	Investment Strategy Classification	34903.402	9555.555	.699	3.653	.003

a. Dependent Variable: Average PBT

4.3.2 Investment Strategy and ROA

Regression analysis was conducted to empirically determine whether investment strategies were a significant determinant of returns on assets. Regression results in table 4.8 indicated the goodness of fit for the regression between investment strategy and returns on assets is satisfactory. An R squared of 0.537 indicates that 53.7% of the variance in ROA is explained by the variances in the investment strategy. The relationship between investment strategy and ROA is positive and significant ($b_1 = 0.092$, p value, 0.001).

Table 4. 7: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.733 ^a	.537	.504	.044150

a. Predictors: (Constant), Investment_Strategy_Classification

Anova statistics confirm these results since the reported probability was 0.001, for investment strategy. The reported probability was less than the convectional probability of 0.05 (5%) significance level.

Table 4. 8: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.032	1	.032	16.253	.001 ^a
	Residual	.027	14	.002		
	Total	.059	15			

a. Predictors: (Constant), Investment_Strategy_Classification

B Dependent Variable: Average_ROA

Results in table 4.10 revealed that there is a positive and significant relationship between the investment strategy and ROA. This was evidenced by a regression coefficient of 0.092. The associated p value (sig) was 0.001.

Table 4. 9: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.006	.033		.169	.868
	Investment Strategy Classification	.092	.023	.733	4.032	.001

a. Dependent Variable: Average_ROA

4.4 Summary and Interpretation of Findings

The study sought to find the preferred type of investment strategy .The study findings in table 4.3 indicate that the statement measuring the preference to an aggressive strategy “The firms focus on high risk high return investments in the short to medium term” attracted a mean score of 4.5 for active firms and 1.67 for passive firms. The findings concur with those in Schoenfeld and Steven (2004) who found that investors who prefer an aggressive investment strategy focus on high return investments in the short to medium term.

Results indicate that active firms had a mean score of 4.1 while passive firms had a score of 1.67 on the statement measuring preference of an aggressive strategy “The firm aims at outperforming the market with its investment portfolio through quick adjustments”. The findings agree with those in Schoenfeld and Steven (2004) who noted that firms that prefer an aggressive investment strategy aim at outperforming the market with their investment portfolio through quick adjustments.

Results further indicate that active firms had a mean score of 4.20 while passive firms had a score of 2.17 on the statement measuring preference of a value strategy “The firm conducts market research and invests in undervalued stocks”. The findings agree with those in Jones (2009) who noted that firms who prefer value strategy invest after detailed research and analysis of the company and the industry.

Results indicate that active firms had a mean score of 3.70 while passive firms had a score of 2.67 on the statement measuring preference of a value strategy “The firm assumes that the market is yet to realize the potential of various stocks it has identified and once it does, the price will go up significantly”. The findings agrees with those in Jones (2009) which noted that firms preferring a value strategy assume that the market is yet to realize the potential of the stock and once it does, the price will go up significantly.

Results indicate that active firms had a mean score of 4.00 while passive firms had a score of 2.17 on the statement measuring preference of a moderate risk strategy “The Firm attempts to minimize the risk in their portfolio by adding a few stable stocks”. The findings concur with those in Ferri (2009) which stated that firms preferring a moderate risk strategy attempts to minimize the risk in their portfolio by adding a few stable stocks.

Furthermore, results indicated that active firms had a mean score of 3.80 while passive firms had a score of 2.17 on the statement measuring preference of a moderate risk strategy “The firm balances out the high risk stocks in their portfolio and keep their investment from being wiped out in case the markets go into a nosedive”. The findings agree with those in Ferri (2009) who noted that firms preferring a moderate risk strategy balance out the high risk stocks in their portfolio and keep their investment from being wiped out in case the markets go into a nosedive.

Results also indicate that active firms had a mean score of 3.00 while passive firms had a score of 4.33 on the statement measuring preference of a conservative strategy “The firm seeks out a consistent and dependable income rather than huge profits that come through higher risks”. The findings rhyme with those in Fama & French (1992) which stated that investors who prefer a conservative strategy seek a consistent and dependable income rather than huge profits that come through higher risks.

Results indicate that active firms had a mean score of 3.10 while passive firms had a score of 4.50 on the statement measuring preference of a conservative strategy “The firm clientele is mainly composed of retirees who adopt a conservative investment approach to make sure they do not lose their savings and who prefer to invest in blue chip companies”. The findings correspond with those in Fama & French (1992) which affirmed that firms preferring a conservative strategy tend to attract many retirees who adopt the conservative investment approach to make sure they do not lose their savings through rash investment decisions, yet get decent returns to pay the bills. Blue chip stocks are the best option for these investors.

Results indicate that active firms had a mean score of 3.60 while passive firms had a score of 4.00 on the statement measuring preference of a high risk aversion1 “The firm hesitates to make purchases even in market conditions show definite bullish tendencies”. The findings agree with those in Ferri (2009) which stated that investors preferring a high risk aversion hesitate to make purchases even in market conditions showing definite bull tendencies.

Finally, results indicate that active firms had a mean score of 2.30 while passive firms had a score of 3.33 on the statement measuring preference of a high risk aversion1 “The firm holds back because of fear of losing money and thus fails to make the most of the stock market movements”. The findings rhyme with those in Ferri (2009) which noted that firms that prefer a high risk aversion hold back because of fear of losing money and thus fail to make the most of the stock market movements

Regression analysis was conducted to empirically determine whether investment strategies were a significant determinant of profit before tax. Regression results in table 4.5 indicated the goodness of fit for the regression between investment strategy and profit before tax is satisfactory. An R squared of 0.488 indicates that 48.8% of the variance in PBT is explained by

the variances in the investment strategy. The relationship between investment strategy and PBT is positive and significant ($b_1 = 34\,903.4$, p value, 0.003). This implies that pursuing a passive strategy yields superior Profitability (PBT) compared to Active strategy.

Regression analysis was conducted to empirically determine whether investment strategies were a significant determinant of returns on assets. Regression results in table 4.8 indicated the goodness of fit for the regression between investment strategy and returns on assets is satisfactory. An R squared of 0.537 indicates that 53.7% of the variance in ROA is explained by the variances in the investment strategy. The relationship between investment strategy and ROA is positive and significant ($b_1 = 0.092$, p value, 0.001). This implies that pursuing a passive strategy yields superior Return on Assets (ROA) compared to Active strategy.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

Chapter one discussed the problem statement and the objectives of the study. The study aimed to determine the effect of investment strategies on the financial performance of collective investment schemes in Kenya

Chapter two discussed the literature review, that is, the theories backing the study. The empirical evidence of the study was also given.

Chapter three presented the research methodology. The chapter discussed the type of research design, population, and target population, sampling frame, sample, sample size, sampling technique, instruments to be used, pilot test and data analysis.

Chapter four presented the findings. Regression analysis was conducted to empirically determine whether investment strategies were a significant determinant of profit before tax. Regression results indicated the goodness of fit for the regression between investment strategy and profit before tax is satisfactory. An R squared of 0.488 indicates that 48.8% of the variance in PBT is explained by the variances in the investment strategy. The relationship between investment strategy and PBT is positive and significant ($b_1 = 34\,903.4$, p value, 0.003).

Results further revealed that there is a positive and significant relationship between the investment strategy and PBT. This was evidenced by a regression coefficient of 30903.402. The associated p value (sig) was 0.003.

Regression analysis was conducted to empirically determine whether investment strategies were a significant determinant of returns on assets. Regression results indicated that the goodness of fit for the regression between investment strategy and returns on assets is satisfactory. An R squared of 0.537 indicates that 53.7% of the variance in ROA is explained by the variances in the investment strategy. The relationship between investment strategy and ROA is positive and significant ($b_1 = 0.092$, p value, 0.001).

Results revealed that there was a positive and significant relationship between the investment strategy and ROA. This was evidenced by a regression coefficient of 0.092. The associated p value (sig) was 0.001.

5.2 Conclusions

Following the study findings, it was possible to conclude that all the investment firms adopted two types of strategy which are passive and active. However they further categorized this into five categories which included aggressive, value, moderate risk, conservative and high risk aversion strategies.

The study concluded that 10 firms pursued an active strategy. These firms focus on high return investments in the short to medium term. To achieve these high returns, they are willing to take higher risk. They aim at outperforming the market with their investment portfolio through quick adjustments. These firms also hope to get lucky with a surprise dark horse investment. They invest after detailed research and analysis of the company and the industry. Their assumption is that the market is yet to realize the potential of the stock and once it does, the price will go up significantly. These firms sometimes hit upon a gold mine stock and make a huge profit. The 10 firms also attempt to minimize the risk in their portfolio by adding a few stable stocks. These balance out the high risk stocks in their portfolio and keep their investment from being wiped out in case the markets go into a nosedive. The passive firms tend to make lower profits but get more stability in the portfolio. They are somewhat protected against the volatility of the market.

The study concluded that 6 firms pursued passive investment strategies. Even in market conditions showing definite bull tendencies, passive firms hesitated to make purchases. The passive firm seeks out a consistent and dependable income rather than huge profits that come through higher risks. The firm clientele is mainly composed of retirees who adopt a conservative investment approach to make sure they do not lose their savings and who prefer to invest in blue chip companies

It was also possible to conclude that investment strategies had a positive and significant relationship with financial performance of investment firms. It was possible to conclude that there was a positive relationship between investment strategy and profit before tax.

It was also possible to conclude that there was a positive relationship between investment strategy and return on assets.

It was possible to conclude that pursuing a passive strategy yields superior Profitability (PBT) compared to Active strategy. Furthermore, the study concluded that pursuing a passive strategy yields superior Return on Assets (ROA) compared to Active strategy.

5.3 Policy Recommendations

From the study findings, it was recommended that the investment firms to adopt different types of strategies so as to maximize their profitability. These strategies include active, passive, aggressive, value, moderate risk, and conservative and high risk aversion strategies.

It was also recommended that the investment firms to pursue passive strategy because it yields superior profitability than active strategy. The study also recommends that the firms should pursue passive strategy as it yields superior returns on assets compared to active strategy.

It was also recommended that the investment firms to adopt different forms of investments such as investment property, real estate investments, mutual funds, government securities and equity.

The study recommends that those firms that prefer value strategy to invest after a detailed research and analysis of the company and industry. It was also recommended that the firms that want to minimize the risk in their portfolio by adding a few stable stocks should opt for moderate risk strategy.

The study recommended that firms should be consistent in their investment strategy. Even in market conditions showing definite bull tendencies, passive firms hesitated to make purchases. The passive firm should consistently seeks outs a consistent and dependable income rather than huge profits that come through higher risks. The passive firm should consistently ensure that the clientele is mainly composed of retirees who adopt a conservative investment approach to make sure they do not lose their savings and who prefer to invest in blue chip companies.

Finally, the study recommends that those firms that tend to attract many retirees who adopt the conservative investment approach to make sure they don't lose their savings through rash investment decisions yet get decent returns to pay the bills should invest in conservative strategy.

5.4 Limitations of the Study

The limitations of the study are the challenges or difficulties that face the researcher during the research exercise. One of the limitations of this study included a possibility of uncooperative respondents, scope coverage and other related issues that complicated availability of information. The researcher, however, made generalizations subject to these limitations.

Another limitation was that there were confidentiality issues in this study like the withholding of crucial information by the respondents. Consequently, there were difficulties in getting the staff and management of investment firms to fill in the questionnaires due to erratic schedules in the firms. However, the researcher addressed those issues by first creating a good rapport with the senior management that helped in getting their staff fill the questionnaires.

The researcher had also to explain the importance of the study and to reassure the respondents that the information given would not be used in any way against them so as to win the acceptance of the respondents.

The other limitation was on the issue of schedules the researcher had to visit several times and wait till late in the evening so as to get hearing of the staff.

5.5 Suggested Areas for Further Study

Further studies need to be conducted on the factors that affect the achievement of the goals, objectives and strategies. This may shed light on the reasons why the collective investment schemes have not achieved their objectives of financial performance.

In addition, a study on the critical success factors (CSF) for the collective investment schemes sector may also be necessary so that the management may have insights on what to concentrate on. That is, such a study would help to identify the critical few out of the trivial many.

Further studies should focus on the effect of corporate governance mechanisms on the performance of collective investment schemes. It may be important to evaluate whether the separation of powers between chairman and CEO, the existence of internal audit, and debt covenants.

Future areas of studies should concentrate on other factors that influence performance of collective investment schemes. For instance, competition, the industry structure, resources and capabilities of the organization.

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Appendices

Appendix 1 : Questionnaire

Dear Respondent,

THE EFFECT OF INVESTMENT STRATEGIES ON THE PERFORMANCE OF INVESTMENT FIRMS IN KENYA

A. ORGANIZATION INFORMATION

1. How long have your firm been in existence (tick as appropriate)
- a. Less than 1 yr
 - b. Btw 1-5 yrs
 - c. Btw 5-10 yrs
 - d. Over 10 yrs

SECTION B: INVESTMENT STRATEGIES

2. This section attempts to identify the investments strategies that the firm utilizes. Please state your level of agreement or otherwise with the following statements. Use the following likert scale. *Strongly Agree=5, Agree=4, Neither Agree nor Disagree=3, Disagree=2, Strongly disagree=1*

	<i>Strongly disagree</i>	<i>Disagree</i>	<i>Neither Agree nor Disagree</i>	<i>Agree</i>	<i>Strongly Agree</i>
	1	2	3	4	5
1. The firms focus on high risk high return investments in the <u>short</u> to <u>medium</u> term.					
2. The firm aims at outperforming the					

	<i>Strongly disagree</i>	<i>Disagree</i>	<i>Neither Agree nor Disagree</i>	<i>Agree</i>	<i>Strongly Agree</i>
	1	2	3	4	5
market with its investment portfolio					
3. The firm conducts market research and invests in undervalued stocks					
4. The firm assumes that the market is yet to realize the potential of various stocks it has identified.					
5. The Firm attempts to minimize the risk in their portfolio by adding a few stable stocks					
6. The firm balances out the high risk stocks in their portfolio.					
7. The firm seeks out a consistent and dependable income.					
8. The firm clientele is mainly composed of retirees.					
9. The firm hesitates to make purchases even when market conditions show definite bullish tendencies.					
10. The firm holds back because of fear of losing money and thus fails to make the most of the stock market movements.					

11. What other investment strategies are utilized by your firm?

a) _____

DO NOT FILL-TO BE OBTAINED FROM SECONDARY SOURCES

SECONDARY DATA

C: TYPE OF INVESTMENTS UNDERTAKEN BY THE COMPANY

12. This section attempts to identify the type of investments that the firm undertakes. Please indicate the value

	Value in million ksh
Local stocks	
International equity	
cash equivalents	
Bonds	
Real estate properties	
Futures and Options	
Investment in associates and subsidiaries	

13. What other investments are included in the investment portfolio?

a) _____

D: FINANCIAL PERFORMANCE

14. The following ratios are to be obtained from the financial statements of Investment firms or CMA

Investment Company	Year	Profit Before Tax (PBT)	Return on Assets (ROA)
	2006		
	2007		
	2008		
	2009		
	2010		
	2011		

Thank you

Appendix 2: CMA Approved CIS (CMA, 2011)

	CIS
1	African Alliance Kenya unit trust scheme
2	Old Mutual Unit Trust scheme
3	British American Unit Trust Scheme
4	Stanbic Unit Trust Scheme
5	Commercial Bank of Kenya Unit Trust scheme
6	Zimele Unit Trust scheme
7	Suntra Unit Trust scheme
8	ICEA Unit Trust Scheme
9	Standard Investment Trust funds
10	CIC Unit Trust Scheme
11	Madison Asset Unit Trust Funds
12	Dyer and Blair Unit Trust Scheme
13	Amana Unit Trust Scheme
14	CFC Unit Trust Fund
15	Diaspora Unit Trust Scheme
16	First Ethical Opportunities Fund