FACTORS THAT INFLUENCE DIVERSIFICATION STRATEGIES OF INSURANCE COMPANIES IN KENYA

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DECLARATION

I declare that this is my original work and has not been presented for a degree thesis/project any other university.

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D 61/7385/2006

Sign: ………………………………… Date: ………………………

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

Sign: ……………………………… Date: ………………………….

FLORENCE MUINDI

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I wish to thank my supervisor, Florence Muindi, for her guidance towards completion of this project. I also thank all staff at the School of Business, University of Nairobi, friends and colleagues at work place for their support during my studies. Finally, I wish to thank the almighty God for giving me courage and perseverance to complete this project.

DEDICATION

I dedicate this research projects to my parents parent and beloved family who have been of great assistance through out my studies. God bless you.

ABSTRACT

Diversification involves the entry of a company into new lines of activity through a process of internal development or through acquisition, which entails changes in its administrative structure, system or other management procedures. Many firms use diversification as a way to reduce risk by investing in a variety of assets or business ventures. Diversification can offer companies many advantages such as cost reduction, reduction in asset depreciation and risk reduction. Other advantages involve synergies or the expansion of business, creation and improvement of long-term strategic assets and long-term sustainability and regional development through resource diversification.

The objective of the study was to determine the factors that influence diversification strategies adopted by mainstream insurance companies in Kenya. This study adopted a cross-sectional survey research design. The study will target all insurance companies in Kenya and semi structured questionnaires were used to collect primary data from top managers in charge of marketing from each of the insurance companies, Data analysis was done by use of descriptive statistics such as frequencies, percentages, mean scores and standard deviations.

The findings of the study revealed that diversification by mainstream insurance companies in Kenya is influenced by availability of finances, government regulatory policies, attractiveness of the industry and/or market, entry costs in insurance industry, access to distribution channels for insurance services and availability of workforce resources, business risk due to uncertainty in the new markets, limited knowledge of the new services, lack of human resource to facilitate investment in new service or market, increased competition due to new entrants in the insurance industry, change in information communication technology, difficulty in determination of the present or future value of the firm and difficulty in making diversification. The study recommends that insurance companies should invest in feasibility studies aimed at analyzing the factors that influence diversification strategies and conduct regular monitoring and evaluation intended to measure the effectiveness of the adopted diversification strategies.

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CHAPTER ONE: INTRODUCTION

1.1 Background to the Study

Diversification is a way to reduce risk by investing in a variety of assets or business ventures (Zhou, 2008). Diversification is thus a common and fundamental concept in both daily life and business. To obtain the optimal strategy of diversification, the risk must be defined and the associated investment opportunities modeled (Zvi *et al.,* 2009). In addition, the utility or investor's risk tolerance and investment horizon must be specified. In terms of asset allocation and portfolio choice, the risk is usually defined as the standard deviation of the portfolio return (Hong, 2008). This measures the variability of the return relative to the expected value of the return. Given a fixed level of expected return, the strategy that generates the minimum variance is preferred. To achieve this, the optimal diversification among the assets will usually be required. The risk tolerance of an investor determines the trade-off between return and risk, as well as the level of risk to take (Zvi *et al.,* 2009).

Diversification has not only been one of the main topics of interest within strategic management research, but has also received the attention of historians, economists and researchers in such areas as finance, law, marketing and public policy (Hoskisson and Hitt, 1990; Ramanujam and Varadarajan, 1989). Diversification can be defined as the entry of a company into new lines of activity through a process of internal development or through acquisition, which entails changes in its administrative structure, system or other management procedures. Within this definition is implicit the assumption that the decision of the company to enter a new business is linked to the choice of the entry mode into that business.

Diversification can offer companies many advantages. From a financial point of view, they include cost reduction, asset depreciation and risk reduction (Bergh, 1997). Strategic advantages involve synergies or the expansion, creation and improvement of long-term strategic assets (Li and Greenwood, 2004; Markides and Williamson, 1994). These advantages are particularly evident in the tourism sector: synergies, cost sharing, risk

reduction or brand improvement. In addition, resource diversification contributes to long-term sustainability and regional development (Ivars, 2003).

1.1.1 Diversification Strategy

Any company's strategic emphasis is increasing sales volumes, boosting market share and cultivating a loyal clientele. Organizations pursue opportunities for geographical market diversification. The natural sequence for geographical diversification is local to regional to national to international. The degree of penetration will however differ from area to area depending on the profit potentials (Thompson and Strickland, 1993). The strategies of diversification can include internal development of new products or markets, acquisition of a firm, alliance with a complementary company, licensing of new technologies, and distributing or importing a products line manufactured by another firm. Generally, the final strategy involves a combination of these options. This combination is determined in function of available opportunities and consistency with the objectives and the resources of the company (Machel, 1972)

There are three types of diversification, Concentric, Horizontal and Conglomerate. In the concentric diversification, the organization adds new products or services which have technological or commercial synergies with current products and which will appeal to new customer groups (Machel, 1972). In the horizontal diversification there is production of new products and services that do not refer to the current business activity but are offered to the current customer (Ticha & Hron 2007). In the conglomerate (mixed) diversification, the organization produces new products and services that do not refer to the current business (Ticha & Hron 2007).

1.1.2 Factors Influencing Diversification Strategy

Diversification is influenced by several factors. These include financial health attractiveness of the industry and/or market, availability of workforce resources and government regulatory policies. Availability of finances is important because diversification requires financial outlays of significant size. Firms should have sufficient resources that cater for different initiatives undertaken during diversification as well as

ensuring that existing business activities are functioning effectively (Steven and Marks 1998). Attractiveness of the industry and/or market is importance because diversification into an industry or market that is not performing well due to general economic conditions or local problems can result in a significant loss of income and security (Mintzberg and Quinn, 1992). Moreover, government regulatory policies impact on the diversification decision. Government can limit or even foreclose entry into industries with such controls as licensing requirements (Porter, 1980).

Diversification can also be influenced by factors such as dynamic capabilities, knowledge searching and institutional environment. Doving and Gooderham (2008) demonstrated that dynamic capabilities have a distinct impact on the scope of services provided by a firm. Pennings *et al.,* (1994) stated that a firm's expansions are more persistent when they are related to its core skills and when it has a higher level of diversification experience, underscoring the importance of organizational learning and search for knowledge. Institutional environment is also important in diversification because business groups consist of individual firms that are associated by multiple links such as cross-ownership, close market ties and social relations through which are coordinated to achieve business objectives (Yiu et al., 2007).

1.1.3 The Kenya Insurance Industry

The insurance industry in Kenya is quite competitive and crowded. According to Olotch, (1999) the number of players in the Insurance industry was relatively large. There are Fourty Three (43) insurance Companies in a small market of about Kshs. 20 Billion. He noted that the Republic of South Africa accounted for more than 90% of the premium in Africa and had half the number of insurers listed in Kenya. He further suggested that the local Insurance Companies in Kenya should merge to create bigger but fewer units (Olotch, 1999). The industry is governed by the Insurance Act and is regulated by the Insurance Regulator

Forty one insurance companies and three reinsurance companies are currently licensed to operate in Kenya. Due to the presence of many players in the market, competition for business has unfortunately focused on pricing. In a survey carried out for the period 2003

to 2005, the market produced positive underwriting results despite the pressure on rates. Over these three years, nineteen companies averaged a combined ratio of under 100%, signifying underwriting profit, while the remaining sixteen companies showed underwriting losses, with the worst performer recording a combined ratio of 135%. In spite of this, all but two companies were able to realize a profit for year 2005 because healthy investment returns boosted the poor underwriting performance. As a result of price wars and other management inadequacies, the industry experienced company failures, with five companies being placed under liquidation or statutory management. The issue of price competition has been of such concern to market players in the industry (short-term business) over the last few years that the Association of Kenya Insurers was forced to give guidance to its members. In place of such competition and failure in the sector, players in the industry need to adopt diversification strategies that will minimize the chance of loss to the company.

1.2 Statement of the Problem

Diversification is a form of growth marketing strategy for an organization and seeks to increase profitability through greater sales volume obtained from new products and new markets. Wan and Hoskisson (2003) and Wan (2005) posit that high levels of diversification improve firm performance even when a country's institutional environment is inadequately developed. Diversification is, however, influenced by several factors such as financial health (Steven and Marks 1998), attractiveness of the industry and/or market (Mintzberg and Quinn,1992), availability of workforce resources (Machel, 1972) and government regulatory policies(Porter, 1980), dynamic capabilities of the firm (Doving & Gooderham (2008), knowledge searching (Pennings *et al.,* 1994) and institutional environment (Yiu et al., 2007).

According to a Moggi & Tessier (2001), there has seen a positive growth of the insurance sector in Kenya since the late 1990s. With the rapid pace of change, companies that succeed are those that adopt more flexible business models and quickly identify new distribution channels. With the increased competition that results in companies diversifying their products and services in order to gain competitive advantage and

improve financial performance, there is a need for evaluation of factors that influence diversification strategies in the context of Kenyan insurance industry.

Previous studies that have been done in Kenya have not focused on has focused on diversification strategies of insurance companies, for example, Kasoma (2000) and Megwa (2005) studies concentrated on the level and impact of technology on insurance companies, Thuo, (2002) analyzed the diversification strategy of Kenya-Re. This study, therefore, intended to fill this knowledge gap by determining the factors that influence diversification strategies adopted by mainstream insurance companies in Kenya.

1.3 Objective of the Study

The study seeks to determine the factors that influence diversification strategies adopted by mainstream insurance companies in Kenya

1.4 Value of the Study

The study findings on diversification strategies adopted by insurance companies will be beneficial to managers of the insurance companies. The mangers will use the findings as basis for formulation of diversification strategies that will enable their companies to take the advantage of the opportunities available and expand their services.

The government of Kenya will also find the findings of the study very valuable. The government regulators and policy makers within the insurance sector such as Insurance Regulatory Authority and Ministry of Finance among others gain insights on the diversification strategies hence use the findings as basis a guide in regulation and policy development.

The findings of this study will make a contribution to the existing literature on diversification strategies. Researchers and academicians will therefore use the study findings as reference during future studies on diversification strategies particularly in regard to insurance sector.

CHAPTER TWO: LITERATURE REVIEW

2.1 Diversification.

The main purpose of diversification is to allow an organisation to grow (Grant, 2005; Thomas and Mason, 2006). Diversification strategically takes the organisation away from its current markets and products with the overall intention to increase the diversity that must be overseen by the organization. International Business Machines (IBM) provides a good example of an organization that has pursued diversification in a purposeful and vigorous manner (Strategic Direction, 2005). Up until the 1980s, IBM enjoyed a virtual monopoly in hardware but this changed very rapidly with increased competition. Diversity in all its implications became the central driver for IBM from 1995 onwards. Diversification included both reviewing the inputs (with the diversification of the workforce) and the outputs (with the move away from products towards services and solutions).

One of the main advantages of diversification identified in the management literature is the synergy that it creates (Ensign, 1998). By moving into new areas, opportunities emerge to develop new inter-relationships through the actual process of working on new services and markets. This synergy makes it is possible to produce a combined return on resources that is greater than the sum of the parts. The likely success of the diversification strategy will be the fit between the different business units and their working relationships. The impetus is on the managers of the different units to understand their inter-relationships so the probability of synergy can be increased.

According to Calori and Harvatopoulos (1988), there are two dimensions of rationale for diversification. First, the diversification may be defensive or offensive. Defensive reasons may be spreading the risk of market contraction, or being forced to expand when current product or current market orientation seems to provide no further opportunities for growth. Offensive reasons may be conquering new positions, taking opportunities that promise greater profitability than diversification opportunities, or using retained cash that exceeds total diversification needs. The second dimension involves the expected outcomes of diversification. Management may expect great economic value (growth,

profitability) or first and foremost great coherence and complementarities with their current activities (exploitation of know-how, more efficient use of available resources and capacities). In addition, companies may also explore diversification just to get a valuable comparison between this strategy and diversification.

Diversification strategies are used to expand firms' operations by adding markets, products, services, or stages of production to the existing business. The purpose of diversification is to allow the company to enter lines of business that are different from current operations. When the new venture is strategically related to the existing lines of business, it is called concentric diversification. Conglomerate diversification occurs when there is no common thread of strategic fit or relationship between the new and old lines of business; the new and old businesses are unrelated (Thompson & Strickland 1993)

2.2 Diversification Strategies

There are three types of diversification, Concentric, Horizontal and Conglomerate. In the concentric diversification, the organization adds new products or services which have technological or commercial synergies with current products and which will appeal to new customer groups (Machel, 1972). The objective is therefore to benefit from synergy effects due to the complementarities of activities, and thus to expand the firm’s market by attracting new groups of buyers. Concentric diversification is to a great extent focused on the optimal usage of the existing production factors; let us say those which represent the competitive advantage of an organization.

In the horizontal diversification there is production of new products and services that do not refer to the current business activity but are offered to the current customer (Ticha & Hron 2007). The organization adds new products or services that are technologically or commercially unrelated to current products, but which may appeal to current customers. In a competitive environment, this form of diversification is desirable if the present customers are loyal to the current products and if the new products are of good quality and are well promoted and priced. Moreover, the new products are marketed to the same economic environment as the existing products, which may lead to rigidity and

instability. In other words, this strategy tends to increase the firm's dependence on certain market segments (Machel, 1972)

In the conglomerate (mixed) diversification, the organization produces new products and services that do not refer to the current business (Ticha & Hron 2007). The new products or services do not have technological or commercial synergies with current products, but which may appeal to new groups of customers. The main reasons of adopting such a strategy are to improve the profitability and the flexibility of the company and to get a better reception in capital markets as the company gets bigger (Machel, 1972).

2.3 Factors Influencing Diversification.

There are several factors that influence diversification. These include financial health, attractiveness of the industry and/or market, availability of workforce resources and government regulatory policies.

2.3.1 Financial health

Diversification depends on financial health of a firm. Business owners should undertake a comprehensive and clinical review of their present fiscal standing and future prospects before expanding a business into a new area (Steven and Marks 1998). The cost of entry into a market should consider before diversification process start. Diversification, whether through diversification or acquisition, typically requires financial outlays of significant size. A company must have the means to meet new financial requirements while simultaneously keeping the existing business running smoothly (Steven and Marks 1998).

The need for external finance can improve the allocation of capital even in instances in which it introduces inefficiencies at the firm level (Almeida & Wolfenzon, 2004). In the presence of limited pledge ability, outside investors prefer to liquidate a mediocre project because they can only get a fraction of the future return. However, in the absence of external finance, insiders prefer not to liquidate such projects because they keep the full return. For a firm to attract sufficient capital when its financing needs are large, the firm has to commit to liquidate. Thus, firms that need to raise external finance are liquidated

more often than internally financed firms (Diamond, 1991). While excessive liquidation might be suboptimal for a firm in isolation, it may be socially beneficial because the released capital flows from mediocre to high productivity projects and thereby improves capital allocation.

2.3.2 Attractiveness of the industry and/or market

Attractiveness of the industry and/or market is another factor that influences diversification. Analysts attach varying level of importance to this factor. Diversification into an industry or market that is dragging, whether because of general economic conditions or local problems, can result in a significant loss of income and security. As Mintzberg and Quinn (1992) observed, some businesses attach little significance to this, relying instead on vague beliefs that the industry or market is a good fit with its existing operations. Other businesses ignore the attractiveness test due to low entry cost. Sometimes the buyer has an inside track or the owner is anxious to sell. Even with a low price, a one-shot gain will not offset a perpetually poor business. Besides, some businesses mistakenly interpret recent market or industry trends as indications of long term health (Mintzberg and Quinn (1992).

Dimensions of market attractiveness include market size/potential (Brewer, 2001; Papadopoulos *et al.,* 2002) and market development (Day *et al.,* 1988). Market size/potential has to do with the size of the market and the amount of sales, profits, etc. that can be obtained from entry and throughout the presence of firms in that market or in a planning period (Sakarya *et al.,* 2007). Market development captures the quality of the market in terms of its socio-economic advancement or progress. Aspects such as per capita income and employment rates are believed to reflect levels of market development. Managers can use industry and product specific criteria to operationalize both dimensions (market size/potential and market development) and readily identify the specific attractiveness of markets related to their businesses.

2.3.3 Availability of workforce resources

Availability of workforce resources is another factor to be considered. When considering diversification, companies need to analyze the ways in which such a step could impact their current employee work forces (Machel, 1972). Access to distribution channels should also be considered. A company engaged in introducing a new product into the market should first ensure they have adequate access to distribution channels within the targeted market. The more limited the wholesale or retail channels for a product are and the more existing competitors have these tied up, obviously the tougher entry into the industry becomes Porter (1980) in Competitive Strategy: Techniques for Analyzing Industries and Competitors. Existing competitors may have ties with channels based on long relationships, high-quality service, or even exclusive relationships in which the channel is solely identified with a particular manufacturer. Sometimes this barrier to entry is so high that to surmount it a new firm must create an entirely new distribution channel (Porter, 1980)

2.3.4 Government regulatory policies

Government regulatory policies at the local, state and national level can also have an impact on the diversification decision. Government can limit or even foreclose entry into industries with such controls as licensing requirements and limits on access to raw materials (Porter, 1980). Regulatory controls on air and water pollution standards and product safety and efficacy should also be weighed. Pollution control requirements can increase the capital needed for entry and the required technological sophistication and even the optimal scale of facilities. Standards for product testing, common in industries like food and other health-related products can impose substantial lead times, which not only raise the capital cost of entry but also give established firms ample notice of impending entry and sometimes full knowledge of the new competitor's product with which to formulate retaliatory strategies. Many of these regulations, while enormously beneficial to society, can have a bearing on the ultimate wisdom of a diversification strategy (Porter, 1980).

2.3.5 Dynamic capabilities,

The concept of dynamic capabilities (Helfat & Peteraf, 2003; Makadok, 2001) had significant implications for research on diversification that emerged in the late 1990s and early 2000s. This line of research focused on the dynamic perspective of resources and capabilities to inform diversification or corporate scope largely from a temporal perspective. For example, Galunic and Eisenhardt's (2001) study viewed corporate divisions as combinations of capabilities and product market areas of responsibilities that may be recombined in various manners. Helfat and Eisenhardt (2004) examined how inter-temporal economies of scope, achieved by redeploying resources and capabilities between related businesses over time as firms exit some markets while entering others, help firms diversify into related businesses.

Doving and Gooderham (2008) demonstrated that dynamic capabilities have a distinct impact on the scope of services. Using the concept of corporate coherence, which is conceptualized as a dynamic interconnectedness between a firm's technological competencies and its downstream activities, Piscitello (2004) showed that firm performance is positively influenced by corporate coherence. Approaching the relationship between resources/capabilities and diversification from a dynamic perspective, thereby incorporating the elements of change and interdependence into the mix, has led to a richer understanding of the diversification process and subsequent performance implications.

2.2.6 Knowledge searching

Another important moderator of corporate diversification is knowledge searching. Miller (2006) emphasized how a firm's knowledge base interacts with its product market activity. Miller, Fern, and Cardinal (2007) examined the impact of sources of knowledge on technological innovation within diversified firms. The findings by Pennings *et al.,* (1994) demonstrated that a firm's expansions are more persistent when they are related to its core skills and when it has a higher level of diversification experience, underscoring the importance of organization learning and searching.

Chang (1996), drawing upon the knowledge-based view, argued that the firm engages in continuous search and selection activities to improve its knowledge base and thus improve its performance. His study demonstrated that the firm's knowledge base is useful for predicting which businesses a firm enters or exits. Mosakowski's (1997) stated that diversification can be understood as a process through which firms search for the best use of their resources. Viewed from this perspective, diversification not only may be a result of excess resources but can be viewed as a process of searching for the best use of a firm's resources across different industries or market segments.

2.2.7 Institutional environment.

Institutional environment is a core component in diversification and incorporating this element into the diversification literature is likely to generate alternative conclusions to the received knowledge of corporate diversification (Greif, 2006). Business groups consist of individual firms that are associated by multiple links, potentially including cross-ownership, close market ties (such as inter-firm transactions), and/or social relations (family, kinship, or personal friendship ties) through which they coordinate to achieve mutual objectives (Yiu *et al.,* 2007). To account for the rise of business groups in emerging economies, Guillén (2000) and Kock and Guillén (2001) argued that this phenomenon is largely the result of firms accumulating the capability of repeating entry into new businesses, which can be viewed as valuable, rare, and inimitable. In a study on the potential benefits of chaebols (Korean business groups), Chang and Hong (2000) emphasized the within-group resource-sharing and internal business transactions. Yiu *et al.,* (2005) employed the resource based and institutional perspectives to examine how Chinese business groups acquire resources and capabilities to prosper. They found that group firms' behaviors may differ from those of non-group firms. In addition, Belenzon and Berkovitz's (2010) showed that group firms are more innovative than are non-group firms, especially in industries that rely more on external funding and in groups with more diversified capital sources.

2.2.8 Information asymmetry

A considerable literature suggests that corporate diversification is a leading example of the agency relationship between shareholders and managers and therefore, diversified firms are subject to larger asymmetric information problems more than focused firms are (Burch and Nanda, 2003; Doukas and Pantzalis, 2003; Scharfstein and Stein, 2000; Rodríguez-Pérez and Van Hemmen, 2010). The source of the difference in asymmetry is that diversified firms are less transparent than focused firms are (Thomas, 2002; Rodríguez-Pérez and Van Hemmen, 2010). For instance, while managers of diversified firms can observe divisional cash flows, outsiders can observe only crude estimates of divisional cash flows. Thus, the problems of account translation and consolidation make company reports less transparent to outsiders, and reported earnings will convey less value-relevant information. To the extent that accounting figures for diversified firms are less transparent compared to those of focused firms, they provide a greater incentive for difficult to detect earnings management.

Research and development (R&D) can increase the problem of information asymmetry, increase agency problems (Hall, 2002) and decrease transparency. Research and development investments can be used to manipulate earnings. In this context, Nagy and Neal (2001) suggest that both USA and Japanese managers use R&D investments to smooth income and that Japanese managers do so at a significantly greater degree. Moreover, the existence of information asymmetry between firm management and firm shareholders is a necessary condition for the practice of earnings management (Dye, 1988). Thus, when information asymmetry is high, stakeholders do not have the necessary information to look through the manipulated earnings. Earnings management also results when shareholders, as is the case for highly diversified firms, have insufficient resources, incentives, or access to relevant information to monitor managerial actions which may intensify the practice of earnings management (Warfield et al., 1995).

2.2.9 Investment misallocation

Investment decisions in diversified firms are known to incur three types of risks. The first is the opportunism in the choice of investment projects (Ahn and Denis, 2004; Goldman, 2005). Diversified firms tend to misallocate their investment funds by cross subsidizing poorly performing divisions. Berger and Ofek (1995), for example, document that diversified firms are prone to cross-subsidize investments in divisions with poor growth opportunities. Consistent with this view, Rajan et al. (2000) model the presence of power struggles among the firm's divisions and show that diversification causes resources to flow to inefficient investments. Similarly, Scharfstein and Stein (2000) explain how rent-seeking divisional managers can subvert the internal capital allocation decision. These studies paint diversified firms as organizations that divert funds from stronger divisions to weaker ones and thereby misallocate their investment capital.

Investment misallocation can result from the possibility that investments and divestitures can satisfy objectives of accounting earnings management and disclosure of desired earnings. Dranikoff *et al.* (2002) argue that the decision to divest is nearly always in response to pressure as the example of the divested business suffering heavy losses, the parent having a suffocating debt burden, or Wall Street analysts turning negative. They indicate that among 50 of the largest divestitures completed over a period of four years, more than three-quarters were completed under pressure, most of them only after long delays, when problems became so obvious that action was unavoidable. Similarly, Haynes *et al.* (2003) suggest that divestment is a purposeful response to financial, corporate governance and strategic variables and, as such, appears broadly consistent with both the agency theoretical and strategic views of the firm.

2.2.10 Cultural diversity

Culture relates to core organizational values. In turn, values are paramount factors to organizations and underpin attitudes, decisions and behavior (Imen & Souad, 2011). An increasing number of successful organizations have, at least partly, attributed their success to effective culture management. The firm can base its employee values on the

principals of respect, integrity, transparency and excellence. Inversely, a firm can make of the pursuit of profit its dominant and even unique value (Arnold and Lange, 2004; Thomas, 2002).

Cultural issues accentuate further agency problems and earnings management in diversified firms. The problem of diversified firms is that they have numerous subsidiaries and that each subsidiary may have a particular culture that can diverge from that of other subsidiaries (Imen & Souad, 2011). The problem of cultural diversity is worsened if industrially diversified firms are also geographically diversified. The faraway operations are more difficult to control, notably because they put firms in contact with other cultures (Sambharya, 1996) and shareholders will be incapable of controlling agents' actions.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Research Design

This study adopted a cross-sectional survey research design. Cross-sectional studies involve observation of a population, or a representative subset, at a defined time (Trochim, 2006). Cross-sectional survey has been chosen because it aims at providing data on the entire population under study. This study involved a census in which all the insurance companies will be studied.

3.2 Target population

The study targeted all the 33 insurance companies that are authorized to operate in Kenya (see appendix ii). The insurance companies selected have wide range of insurance services hence can provide the data on diversification strategies. Top managers in charge of marketing from each of the insurance companies will provide the data required for the study.

3.4 Data Collection

Primary was collected using semi structured questionnaires which was consist of both open ended and close questions. The questionnaires were delivered to the respondent and picked up later. This gave respondent enough time to fill in the questionnaires. The questionnaire had three sections. Section A included demographic data, Section B will included diversification strategy and section C will involved factors influencing diversification strategy

3.5 Data Analysis

The data quantitative data collected was coded and the analysis was done by use of descriptive statistics such as frequencies, percentages, mean scores and standard deviations. The results were presented using tables, graphs and charts for ease of

understanding. The qualitative data was analyzed through content analysis and result presented in prose.

CHAPTER FOUR: ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents the study findings the study whose aim was to determine the factors that influence diversification strategies adopted by mainstream insurance companies in Kenya. The analysis has been done by use of descriptive statistics such as frequencies, percentages, mean scores and standard deviations. This chapter has the study findings presented in tabular forms and graphs.

The study targeted a total of 33 insurance companies. However, the study managed to collect data from 24 insurance companies which accounted for a response rate of 72.7 %. This was considered appropriate for the analysis and subsequent drawing of conclusions. According to Mugenda and Mugenda (2003) a response rate of 50 % is sufficient for a study, 60% is good and 70% is excellent for a study. All the respondents were marketing managers.

4.2 Demographic information

Age and duration of work are determinants of the knowledge, skills and experience that a person in a given field of specialization. Therefore the study established the age and work duration of the respondents who participated in the study. The study findings are illustrated the figures below.

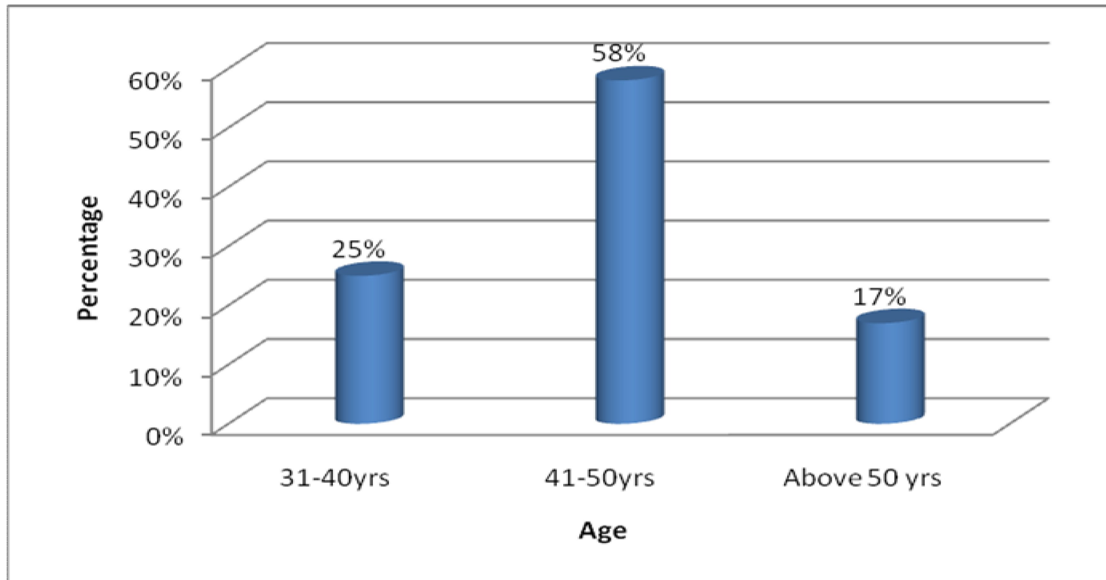
4.2.1 Designation

The respondents were requested to indicate their designation in their insurance companies. The study managed to collect data from marketing manager in all the 24 insurance companies that participated in the study. This reveals that the study managed to collect data from respondents who are knowledgeable on diversification strategies employed by insurance companies.

4.2.2 Age

The respondents were requested to indicate the bracket within which their ages fall. The findings are shown in figure 1 below.

Figure 1: Age

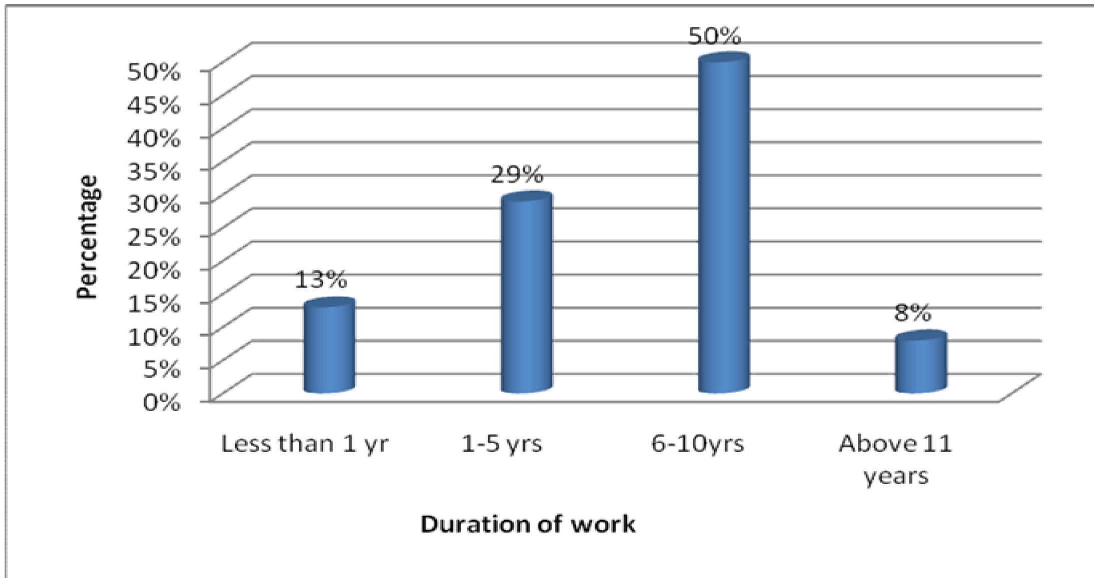


The study findings in figure 1 above indicate that majority of the respondents were aged between 41 and 50 years. The findings reveals that majority of the respondents are old enough to gain knowledge on factors that influence diversification strategies adopted by mainstream insurance companies in Kenya.

4.2.3 Work Experience

The respondents were also requested to indicate the duration of work experience as marketing managers. Figure 2 below illustrates the findings of the study.

Figure 2: Work duration



With respect to the duration of work experience, the findings in figure 2 above revels that majority of the respondents had worked as heads of marketing for insurance companies for a period between 6 and 10 years. The findings indicated that majority of the respondents had worked for time long enough to gain knowledge, skills and substantial experience on factors that influence diversification strategies adopted by mainstream insurance companies in Kenya.

4.3 Diversification Strategies adopted by insurance companies

The study investigated the diversification strategies adopted by insurance companies in Kenya. The respondents were requested to indicate the extent to which their companies had adopted the following diversification strategies. The response was rated on a likert scale of 5 where 1= No extent at all, 2= Less extent, 3= Moderate extent, 4= Great extent and 5= Very great extent. The mean and standard deviations were computed and the results are illustrated in table below.

The responses with a mean less than 1.5 indicated no extent at all, 1.5 to values less than 2.5 indicted less extent, mean from 2.5 to values less than 3.5 indicated moderate extent, mean from 3.5 to values less than 4.5 indicated great extent and means from 4.5 to 5.0 indicated very great extent. The standard deviation indicates how divergent the responses

were from the mean response. A standard deviation more than 1 is significant and shows a great divergence of responses from the mean response.

Table 4.1: Diversification Strategies adopted by insurance companies

Diversification Strategies	Mean	std deviation
Marketing of new services which have technological or commercial synergies with current products and which appeal to new customer groups.	4.256	0.6127
Marketing of new services that are technologically or commercially unrelated to current products, but which appeal to current customers.	4.195	0.7648
Marketing of new services that have no technological or commercial synergies with current products, but which appeal to new groups of customers.	4.062	0.5265
Adoption of new information, communication technologies	3.943	0.4836
Market segmentation	3.845	0.7032
Forming strategic alliances with a complementary company	3.476	0.6248

The study findings in table 4.1 indicate that insurance companies have greatly adopted the following diversification strategies marketing of new services which have technological or commercial synergies with current products and which appeal to new customer groups to great extent with a mean score of 4.256, marketing of new services that are technologically or commercially unrelated to current products, but which appeal to current customers (M=4.195), marketing of new services that have no technological or commercial synergies with current products, but which appeal to new groups of customers (M=4.062), adoption of new information, communication technologies (M=3.943) and market segmentation (M=3.845). Formation of strategic alliances by insurance companies is practiced to a moderate extent as indicated by a mean of 3.476.

The findings of the study revealed a widespread adoption of various diversification strategies by insurance companies. Insurance companies market of new services which have technological or commercial synergies with current products and which appeal to new customer groups. The insurance companies that adopt this diversification strategy enhance their competitive advantage. This diversification strategy enables insurance companies to improve their performance by providing services that attract new customers. The new services enhance customer retention because they bear great similarity to existing services that customers are familiar with.

Moreover, the study finding revealed that insurance companies in Kenya market new services that are technologically or commercially unrelated to current products, but which appeal to current customers. This type of diversification strategy enables insurance companies to utilize innovativeness as a means of enhancing competitive. The new services are designed to suit both current and new customers. Insurance companies adopt develop new products that have better quality but are affordable to the customers.

Insurance companies also market new services that have no technological or commercial synergies with current products but which appeal to new groups of customers. This is aimed at improving financial performance and the ability of an insurance company to provide a wider range of services.

Insurance companies adopt advanced information and communication technologies (as means to enhance quality and efficiency of service delivery. The companies also segment their market according to different needs, financial capabilities and age groups. This enables insurances companies to reach out to all segments of market hence improving financial performance. Formation of strategic alliances by insurance companies also a diversification strategy that is moderately applied by insurance companies. Strategic alliances allows for integration of various marketing strategies that lead to enhanced competitive advantages.

4.4 Factors influencing diversification in insurance companies

The main objective of the study was to determine the factors that influence diversification strategies adopted by mainstream insurance companies in Kenya. To achieve this objective, the respondents were requested to indicate the extent to which the following diversification strategies affect their companies. The results are illustrated in table 4.2 below.

Table 4.2: Factors influencing diversification in insurance companies

Factors influence diversification strategies	Mean	std deviation
Availability of finances	4.425	0.6534
Government regulatory policies	4.216	0.7361
Attractiveness of the industry and/or market	4.073	0.7824
Entry costs in insurance industry	3.986	0.8012
Access to distribution channels for insurance services	3.872	0.6933
Availability of workforce resources	3.865	0.8461

From the study findings illustrated in table 4.2, indicted that diversification in insurance companies is under great influence of availability of finances (M=4.425), government regulatory policies (M=4.216), attractiveness of the industry and/or market(M=4.073), entry costs in insurance industry (3.986), access to distribution channels for insurance services (M=3.872) and availability of workforce resources (M=3.865).

The study findings revealed that diversification strategies are influenced by different factors. Availability of finances is a major factor that influences diversification in insurance industry. For an insurance company to inter into a new market there must be sufficient funds to cater for entry requirements. Besides meeting the cost of entry into a new market, insurance companies must have enough funds to maintain all other operations.

Government regulatory policies are major considerations during diversification in insurance industry. All insurance companies are required to abide by regulatory policies. Insurance companies must fulfill the entry requirement before they are authorized to operate in a given market. In addition to government policies, attractiveness of the market is a major factor that influences diversification in insurance industry. Good financial performance of companies in insurance industries influences the decision of any given company to diversify its services.

The study findings also revealed that access to distribution channels for insurance services influence diversification strategies. Availability of sufficient distribution channels for insurance services encourages insurance companies to diversify their services. Efficient distribution channels for insurance services attract insurance companies which in turn lead to diversification as companies strive to utilize such channels to their advantage.

The study further sought to establish the extent to which the following challenges affect diversification process in insurance companies. The results are illustrated in table 4.3 below.

Table 4.3: Challenges that affect diversification process in insurance companies.

Challenges that affect diversification process in insurance companies	Mean	std deviation
Higher degree of business risk due to uncertainty in the new markets	4.461	0.3126
Limited knowledge of the new services	4.409	0.4132
Lack of financial and human resource to facilitate investment in new service or market	4.328	0.5742
Increased competition due to new entrants in the insurance industry	4.298	0.3645
Difficulty in adjustment to change in information communication technology	3.976	0.7248
Difficulty in determination of the present or future value of the firm	3.804	0.8617

Difficulty in making diversification decisions because they involve many domains	3.769	0.5224

From the study findings illustrated in table, majority of the respondents agreed that diversification in insurance companies is, to a great extent, affected by higher degree of business risk due to uncertainty in the new markets (M=4.461), limited knowledge of the new services (M=4.409), lack of financial and human resource to facilitate investment in new service or market (M=4.328), increased competition due to new entrants in the insurance industry (M=4.298), difficulty in adjustment to change in information communication technology (M=3.976), difficulty in determination of the present or future value of the firm (M=3.804) and difficulty in making diversification decisions because they involve many domains (M=3.769).

The findings of the study revealed that high degree of business risk due to uncertainty in the new markets has an impact on the diversification strategies. Insurance companies may not consider diversification into markets where the industry is not performing well. High business risks tend to discourage businesses from undertaking new investments. Limited knowledge of the new services is another barrier to effectiveness of diversification strategies in insurance industry. When customers are not adequately informed about the new insurance services, they may not subscribe to such services leading to low performance of firm dealing in the affected business.

Lack human resource is a challenge that can hinder diversification strategies by insurance companies. Availability of academically qualified and skilled is a major consideration when an insurance company undertakes to diversify its services. Human capital is important in planning, implementation and evaluation of diversification strategies. Increased competition due to new entrants in the insurance industry also impacts on diversification strategies. When the market is flooded with many firms providing the same service, most of insurance companies tend to adopt various diversification strategies in the effort to increase competitive advantage.

Diversification strategies by insurance companies are also influenced by difficulty in determination of the present or future value of the firm and difficulty in making diversification decisions. Some time managers of insurance companies are faced with the challenge of determining the value of the firm before carrying out diversification. If the value of the firm is not correctly determined, managers may not be able to determine areas that need diversification and allocation of funds may also be challenging.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

This chapter presents the summary of the study findings and conclusion drawn from the study. The chapter also presents recommendations of the study and suggestions for further research.

5.1 Summary of findings

Majority of the respondents were aged between 41 and 50 years and had worked as heads of marketing for their insurance companies for a period between 6 and 10 years. The findings indicated that majority of the respondents were are old and had worked for time long enough to gain knowledge, skills and experience on factors that influence diversification strategies adopted by mainstream insurance companies in Kenya.

The study findings on diversification strategies adopted by insurance companies in Kenya indicate that majority insurance companies in Kenya market new services which have technological or commercial synergies with current products and which will appeal to new customer groups, market new services that are technologically or commercially unrelated to current products but which appeal to current and new groups of customers, adopt new information and communication technologies and carry out market segmentation. However, only a few insurance companies form strategic alliances with a complementary company.

The main objective of the study was to determine the factors that influence diversification strategies adopted by mainstream insurance companies in Kenya. From the study findings majority of the respondents indicated that diversification in insurance companies is influenced by availability of finances, government regulatory policies, attractiveness of the industry and/or market, entry costs in insurance industry, access to distribution channels for insurance services and availability of workforce resources.

Majority of the respondents also indicated that diversification in insurance companies is affected by higher degree of business risk due to uncertainty in the new markets, limited knowledge of the new services, lack of financial and human resource to facilitate investment in new service or market, increased competition due to new entrants in the insurance industry, difficulty in adjustment to change in information communication technology, difficulty in determination of the present or future value of the firm and difficulty in making diversification decisions because they involve many domains.

5.2 Conclusion

The study concludes that diversification by mainstream insurance companies in Kenya is influenced by availability of finances, government regulatory policies, attractiveness of the industry and/or market, entry costs in insurance industry, access to distribution channels for insurance services and availability of workforce resources.

Moreover diversification in insurance companies is affected by higher degree of business risk due to uncertainty in the new markets, limited knowledge of the new services, lack of financial and human resource to facilitate investment in new service or market, increased competition due to new entrants in the insurance industry, difficulty in adjustment to change in information communication technology, difficulty in determination of the present or future value of the firm and difficulty in making diversification decisions because they involve many domains.

5.3 Recommendations

The study recommends that managers in insurance companies should invest in feasibility studies aimed at analyzing the factors that influence diversification strategies. This will enable mangers to formulate appropriate measures which will ensure that objectives of diversification plans are successfully implemented.

The studies also recommend that insurance companies should conduct regular monitoring and evaluation intended to measure the effectiveness of the adopted diversification strategies. This is necessary because insurance companies operate in a dynamic business environment which is highly affected by a variety of factors.

5.3.1 Suggestions for further studies

The study recommends further research on the impact of diversification on financial performance of insurance companies.

Further research should be done on measures taken by insurance companies to enhance effectiveness of diversification.

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APPENDIX 1: Questionnaire

RE: PARTICIPATION IN RESEARCH

I am a postgraduate student pursuing my master degree in Business Administration at the University of Nairobi and conducting a research entitled " Factors That Influence Diversification Strategies of Insurance Companies in Kenya" as one of the major requirements.

In this regard, you have been selected to take part in this study as a respondent. Kindly respond to all items to reflect your opinion and experience. Please answer all the questions freely. You will not be identified from the information you provide and no information about individuals will be given to any organization. The data collected will be used for this academic research only.

Your participation is important for the success of this project and I greatly appreciate your contribution.

Yours Sincerely,

David Githira

SECTION A: RESPONDENT'S PROFILE

1. Please provide responses to the questions below.

a.	Age bracket	18-30 yrs [ ] 31-40yrs [ ] 41-50yrs [ ] Above 50 yrs[ ]
b.	Designation in the insurance company	
c.	Duration of work experience	Less than 1 yr [ ] 1-5 yrs [ ] 6-10yrs [ ] Above 11 years [ ]

SECTION B: DIVERSIFICATION STRATEGIES

2. To what extent has your firm succeeded in implementing the following types of diversification strategies? Tick appropriately using a likert scale of 5 where 5= Very great extent, 4= Great extent 3= Moderate extent and 2= Less extent and 1= No extent at all.

		Very great extent	Great extent	Moderate extent	Less extent	No extent
a.	Marketing of new services which have technological or commercial synergies with current products and which will appeal to new customer groups.					
b.	Marketing of new services that are technologically or commercially unrelated to current products, but which may appeal to current customers.					

c	Marketing of new services that have no technological or commercial synergies with current products, but which may appeal to new groups of customers.					
d	Market segmentation					
e	Forming strategic alliances with a complementary company					
f	Adoption of new information, communication technologies					

3. Which other strategies have been implemented in your firm?
   a)…………………………………………………………………………………..
   b) …………………………………………………………………………………..
   c) …………………………………………………………………………………..
   d) …………………………………………………………………………………..

SECTION B: FACTORS INFLUENCING DIVERSIFICATION STRATEGY

4. To what extent do the following factors influence diversification strategies in your firm? Tick appropriately using a likert scale of 5 where 5= Very great extent, 4= Great extent 3= Moderate extent and 2= Less extent and 1= No extent at all.

		Very great extent	Great extent	Moderate extent	Less extent	No extent
a.	Availability of finances					
b.	Attractiveness of the industry and/or market					
c	Entry costs in insurance industry					
d.	Availability of workforce resources					
e.	Access to distribution channels for insurance services					
f	Government regulatory policies					

5. Which other factors influence diversification strategies in your firm?
   a)…………………………………………………………………………………..
   b) …………………………………………………………………………………..
   c) …………………………………………………………………………………..
   d) …………………………………………………………………………………..
6. To what extent do the following challenges affect diversification process in your firm? Tick appropriately using a likert scale of 5 where 5= Very great extent, 4= Great extent 3= Moderate extent and 2= Less extent and 1= No extent at all.

		Very great extent	Great extent	Moderate extent	Less extent	No extent
a.	Higher degree of business risk due to uncertainty in the new markets					
b.	Limited knowledge of the new services					
c	Lack of financial and human resource to facilitate investment in new service or market					
d.	Adjustment too change in information communication technology					
e.	Increased competition in due to new entrants in the insurance industry					
f	Difficulty in determination of the present or future value of the firm					
	Difficulty in making diversification decisions because they involve many domains					

APPENDIX II: Insurance Companies in Kenya.

1. APA Insurance Company Ltd
2. Africa Merchant Assurance Company Ltd
3. British American Insurance Company Ltd
4. Cannon Assurance Ltd
5. Chartis Kenya Insurance Co. Ltd
6. Concord Insurance Co. Ltd
7. CIC Insurance Group Ltd
8. Corporate Insurance Co. Ltd
9. Fidelity Shield Insurance Co. Ltd
10. First Assurance Co. Ltd
11. GA Insurance Limited
12. Gateway Insurance Co. Ltd
13. Geminia Insurance Co. Ltd
14. Insurance Company of East Africa Ltd
15. Intra Africa Assurance Co. Ltd
16. Invesco Insurance Co. Ltd
17. Kenindia Assurance Co. Ltd
18. Kenya Orient Insurance Co. Ltd
19. Lion of Kenya Insurance Co. Ltd
20. Madison Insurance Co. Ltd
21. Mayfair Insurance Co. Ltd
22. Mercantile Insurance Co. Ltd
23. Occidental Insurance Co. Ltd
24. Pacis Insurance Co. Ltd
25. Phoenix East Africa Assurance Co. Ltd
26. Real Insurance Co. Ltd
27. Tausi Assurance Co. Ltd
28. The Monarch Insurance Co. Ltd
29. The Heritage Insurance Co. Ltd

30. The Kenya Alliance Insurance Co. Ltd
31. Trident Insurance Co. Ltd
32. UAP Insurance Co. Ltd
33. Xplico Insurance Co. Ltd

Source: The Insurance Regulatory Board (2011).