

**A CASE STUDY ON INFLUENCE OF INVESTMENT DIVERSIFICATION ON
FINANCIAL PERFORMANCE OF INVESTMENT FIRMS**

BY

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ABSTRACT

Organizations are operating in environments that are complex and unpredictable. Diversification has assumed position of universality in management process. The relationship between diversification and firm performance has been the subject of abundant research; past studies about effect of diversification on performance have yielded mixed results that are inconclusive and contradictory. The purpose of this study was to establish the influence of investment diversification on financial performance of investment firms; a study of Old Mutual Investment. Specific objectives included: To determine the influence of life assurance policy on financial performance of Old Mutual; to establish the influence of general insurance policy on financial performance of Old Mutual; and to establish the influence of property insurance on financial performance of Old Mutual. The study was guided by Modern Portfolio theory. It adopted a correlation survey research design. The study unit of analysis was Old Mutual whose operations and activities are spread in major towns. The target population was investment firms. The study sample size was Old Mutual Investment Holdings. The study adopted a non-statistical sampling design. Secondary data from financial statements was used. Descriptive statistics was used to summarize and analyze the data; regression analysis was used to assess relationship between variables and ANOVA was used to establish the significance and fitness of the model. Findings showed that life assurance policy does not affect profitability of Old Mutual ($p\text{-value} = 0.007$); general insurance policy affects only 0.1% of Old Mutual profitability ($p\text{-value} = 0.002$) and property insurance policy affects only 0.3% of Old Mutual profitability ($p\text{-value} = 0.007$). P-values from all the independent variables are less than 0.05, meaning strong evidence against the null hypothesis so the null hypotheses of the study are rejected. The study concluded that: Life assurance, General insurance and Property insurance had statistical significant impact on profitability of Old Mutual with a weak positive correlation. The study recommends that firms should diversify more to increase the impact of diversification on profitability. The study suggests that further research on how diversification compares to other grand strategies should be done.

CHAPTER ONE

INTRODUCTION

1.1 Introduction

This chapter consists of background of the study, statement of the problem, research objectives and hypotheses, scope of the study, significance of the study and the conceptual framework.

1.1.1 Background of the Study

Business organizations are operating in environments that are increasingly uncertain, complex, competitive, dynamic and unpredictable. The changes in environments are not only rapid and bewildering; they also appear to be in a state of constant flux. Development arising from these forces and the need for organizations to survive in today fiercely competitive market are causing many organizations to rethink the way they are doing business in order to remain relevant to their stakeholders in the unfolding dispensations. These contextual influences not only present organizations with critical challenges, they also present new opportunities for growth and development. Companies are adopting various strategies to respond to these forces in order to survive and grow. It is important to add that competitive pressures are forcing many organizations to react to these changes with improved quality services and products. In the light of these new challenges, many organizations have played out the logical restructuring paths through the adoption of various performance improvement methodologies ranging from organization development and business acquisitions. Despite the adoption and implementation of these strategic recipes in the past, organizations still find themselves in need of reinvigoration by way of strategic shifting of the organization structure in order to maintain competitive edge and satisfy customers' needs at a profit. The desire for this repositioning has prompted many business organizations to adopt diversification as a corporate strategy.

Zhou (2008) defines diversification as a way employed to reduce risk by investing in a variety of assets or business ventures. Palepu (2005) states that a critical component of a company's strategic management is the diversification strategy and the relationship

between a company's diversification and its economic performance is an issue of considerable interest to the managers as well as to the academicians. In a highly volatile industry it is critical to keep up with competitors through a strategic decision to diversify knowledge of the correct combination of a company's strength and business mix (Teo, 2002). A diversified firm can therefore be defined as one which has operations in more than one industry line or production line, i.e. invests in alternative assets (Ibrahim and Kaka, 2007).

There are diverse arguments based on different studies about diversification (Choi and Russel, 2004, Ofori and Chan, 2000 and Teo and Runeson, 2001). Diversified companies have higher profitability and growth rate as compared to the other companies that are not diversified (Choi and Russel, 2004). Ofori and Chan (2000) however, stands for the opposite by stating that undiversified companies have performed better than their counterparts by remaining focused despite the perceived risk and uncertainties in the business they thrive in. Rumelt (2012) reported that diversifying in related market products gives higher returns than diversifying in unrelated market products. Substantial proportions of companies are always reluctant to diversify and only choose to operate in a single industry despite the claimed potential benefits of diversification (Teo and Runeson, 2001). Nguku (2015) also concludes that diversification in related market products is more beneficial than in unrelated products since it helps in cost cutting, differentiation as well as creates a competitive advantage.

Diversification is a means by which a firm expands from its core business into other product markets Aaker(2010) and Chandler (2010). Research shows corporate management is actively engaged in diversifying activities. Many researchers note a rise in diversified firms Rasheed (2013). European corporate managers according to a survey not only favor it but actively pursue diversification McGraw-Hill (2004).

Diversification, firm size, and executive compensations are highly correlated, which may suggest that diversification provides benefits to managers that are unavailable to investors (Hoskisson and Hitt 2005). Diversification can also lead to the problem of moral hazard, the chance that people will alter behavior after entering into a contract-as in a conflict of interest by providing insurance for managers who have invested in firm

specific skills, and have an interest in diversifying away a certain amount of firm specific risk and may look upon diversification as a form of compensation (Njuguna, 2013).

Diversification can be expensive (Jones & Hill 2001 and Porter, 2012) and place considerable stress on top management (McDougall and Dimanaran 2005).

Literature from the early industrial organization has argued that there is no significant relationship existing between diversification and a firms' performance, meaning that existing firms have no special advantage when entering a new market (Kang et al. 2011). Proctor (2000) states that for a business to survive tough fluctuations in the market, it is wise for it to diversify as this helps in reduction of risk and stimulation of growth to increase profit. Diversification can also be defined as a company's entry into new or untapped markets or even industries to provide new lines of business activities (Chen and Yu, 2011). It is a portfolio strategy designed to cut back risk by combining various types of investments.

There are different types of business diversifications. These include horizontal diversification, vertical diversification, conglomerate diversification, concentric diversification and corporate diversification (Gitau, 2015). Horizontal diversification involves adding similar products to an already existing line of business while targeting the current existing customer groups. On the other hand, vertical diversification involves a business moving either forward or backward of its production cycle for example the production of raw materials or distribution of finished products (Ansoff, 2002).

According to Edwards (2009), concentric diversification entails enlarging the production portfolio by adding new or similar products to an already existing successful line of business. This is usually with aimed at fully utilizing the potential of the existing marketing system and technologies. Contrarily, conglomerate diversification involves companies trying to venture into previously untapped markets thus new products and services that significantly differ from present products and services of an organization are added.

Corporate diversification entails the production of unrelated but definitely profitable goods. It is often tied to large investments where there is an expectation of high return (Rumelt, 2012). Corporate diversification according to Piscitello (2014) has been referred to as the ability of a firm to generate and explore synergies of various types. The central issue on the study of corporate diversification is what determines the direction of firms' diversification, specifically whether to diversify into related or unrelated line of business (Tse, 2000). The ability of a firm to utilize its assets to earn sufficient revenue for long run business sustainability is the reason for concern of financial performance by firm (Pandey, 2007). This then means that a firm's financial performance is measured on the basis of how much wealth it has been able to create for the shareholders at the end of a particular period of concern. Almajali, Alamro & Al-soub (2012) state that there are various measures of financial performance however, most firms adopt financial indicators. Madura (2014) used Return on assets to measure assets efficiency in income generation and this same measure was used by Clarkson, Richardson and Vasvari (2008). Hill, Jones, & Schilling (2015) used Return on Sales but (Higgins, 2012) used Return on Equity to measure financial performance. Hence the statement by Almajali, Alamro & Al-soub (2012) that there are various measures to firms' financial performance. This study will employ the use of ratios and trend analysis in determining the financial performance of a firm. This study used the Return on Equity (ROE) ratios to measure the financial performance of Old Mutual Kenya.

Sayrak (2003) in his research found that diversified firms do not have higher financial performance as compared to the firms dealing in a single product or that which has allocated its capital to production or provision of a single product or service line. On the other hand, a study conducted by Klein (2010) found out that firms that are diversified have a higher financial performance as compared to those that are not, but this study introduced the aspect of environment which this holds in a developing economy where there is high industrial growth.

In a study presenting the theoretical dissimilarities between ability of the firms in United States and the firms in India, Chacar and Vissa (2005) found out that there is similarity in performance of diversified firms in these two countries even though they exist in very opposite ends of economy which is developed and undeveloped economy. Gaur and Kumar (2009) also concluded in their study on link between international diversification and firm accomplishment for emerging economy firms that there is a positive relationship between the two. They went ahead and said that the same relationship is only true for firms operating in a developing economy like India.

Gubbi, Aulakh, Ray, Sarkar and Chittor (2010) argue that there is limited understanding about the value created by unrelated diversification on a firm's financial performance. Purkayastha, Manoloyal, and Edelman (2012) goes further stating that although the connection between unrelated diversification and financial performance has become a significant topic for research in various fields and industries, there is no detailed work of the same research done in developed and emerging markets.

1.1.2 Old Mutual Background

Old Mutual is a wholly owned subsidiary company of Old Mutual plc. It is an international financial services company with expanding operations in life assurance, asset management, banking and general insurance. The company has been in the market since 1845 and is even listed on the London Stock Exchange. Its operations started in Kenya in the late 1920s when a branch was established in Nairobi. In 2002, Old Mutual became the largest private asset management company in Kenya and launched two-unit trust funds in 2003. In 2007, it registered Old Mutual Bond Fund and Muslim Fund. It launched Old Mutual Toboa fund which is a recurring Unit Trust Fund in 2008 and later in 2009 launched RafikiHalisi range of insurance products.

In 2010 Old Mutual acquired a controlling stake in the stock broker reliable securities. Old Mutual has a mission that reads, "through understanding and meeting our customers' needs, we will profitably expand our market for wealth accumulation and protection in Kenya" and a vision that states, "is to be your most trusted savings and wealth management partner in East Africa." Old Mutual values are accountability,

integrity, respect and pushing beyond boundaries. Old Mutual does not just offer investment advice or solutions as well as financial services but also invests in Real Estate Investment Trusts (REIT). This shows that it does not just advise investors to embrace diversification when it comes to investments but it also takes its own advice. In 2016, Old Mutual invested 6.4 Billion Kenya shillings in real estate through a project known as Two Rivers Development Limited (TRDL) which is a project that involves The Two Rivers Mall building sitting on a 10.2 acres piece of land. It is destined to be a world class destination which includes a 3-star hotel being undertaken by city lodge hotel, an office building development, 5-star hotel and residential apartments. Old mutual is also a stock broker in the Nairobi Stock Exchange (NSE), licensed by the Capital Markets Authority. (<http://www.centum.co.ke>, 2018). Old Mutual acquired a majority stake of 60.7 per cent in UAP for Sh25.6 billion (\$253 million) in July 2015 (<http://www.businessdailyafrica.com>, 2017). On financial performance perceptive Old Mutual Kenya increased to £1,216m in 2016, translating to an increase of +1% from 2015 according to the company's annual Report and Accounts 2016 and later experienced a growth of adjusted operating earnings by +25% in 2017.

1.2 Statement of the Problem

The issue of diversification has assumed a position of centrality and universality in the management process. Diversification has become an increasingly important aspect of doing business in the world today. The relationship between diversification and firm performance has been the subject of abundant research in several fields. However, many researchers concurred on the fact that there is no agreement on the precise nature of the relationship between diversification and performance. Some past studies have shown that diversification improves profitability over time; whereas other studies have demonstrated that diversification decreases performance. Another study indicates that no relationship exist between diversification and performance. Studies about effect of diversification on performance have so far yielded mixed results that are inconclusive and contradictory. With contradictory findings of different studies on effect of diversification on financial performance of firms, there exists a knowledge gap. This study therefore sought to bring understanding and expand knowledge in this area to

help clarify the contradictory findings and help reach a definite conclusion. The research problems therefore were; the unavailability of clarity as to whether or not diversification affects firm performance and the existence of increased stiff competition due to small uprising investment firms and banks offering investment and insurance services in the market which might lead to poor financial performance of firms in this industry if no proper strategies are acquired.

1.3 Research Objectives

The major objective of the study was to establish the influence of investment diversification on the financial performance of investment firms, a study of Old Mutual Investment Holdings.

1.3.1 Specific Objectives

The specific objectives of the study were to:

- i. Determine the effect of life assurance policy on financial performance of Old Mutual.
- ii. Establish the influence of general insurance policy on the financial performance of Old Mutual.
- iii. Establish the relationship of property insurance policy on the financial performance of Old Mutual.

1.4 Research Hypothesis

The study was guided by the following research hypotheses:

H_0 : There was no significant relationship between life assurance and financial performance of Old Mutual.

H_0 : There was no significant relationship between general insurance and financial performance of Old Mutual.

H_0 : There was no significant relationship between property insurance and financial performance of Old Mutual.

1.5 Scope of the Study

The study focused on three insurance policies of the Old Mutual Holdings including; life assurance, general insurance and property insurance. This study was focused on utilizing secondary data on the financial performance of the Old Mutual from 2014 to 2017.

1.6 Significance of the Study

The study will have a number of benefits to the policy makers at Old Mutual Kenya as they will have more insights concerning the benefits on diversification and thus keep pursuing the strategy in order to improve their firm performance and gain more competitive advantage. This will assist them to come up with better management alternatives that assist them in proper and effective implementation of diversification strategies. This study will serve as a basis of further research to academicians who are interested in furthering their knowledge on investment diversification.

Also it will be critical in informing investment firms on the impacts of embracing diversification in Kenya, by justifying the importance or otherwise of diversification for investment firms both to the investing firms and stakeholders. Additionally, the study will add to the knowledge that currently exists on investment diversification of firms.

1.7 Conceptual Framework

A conceptual framework is a structure which the researcher believes can best explain the natural progression of the phenomenon to be studied (Camp, 2001).

Independent Variable

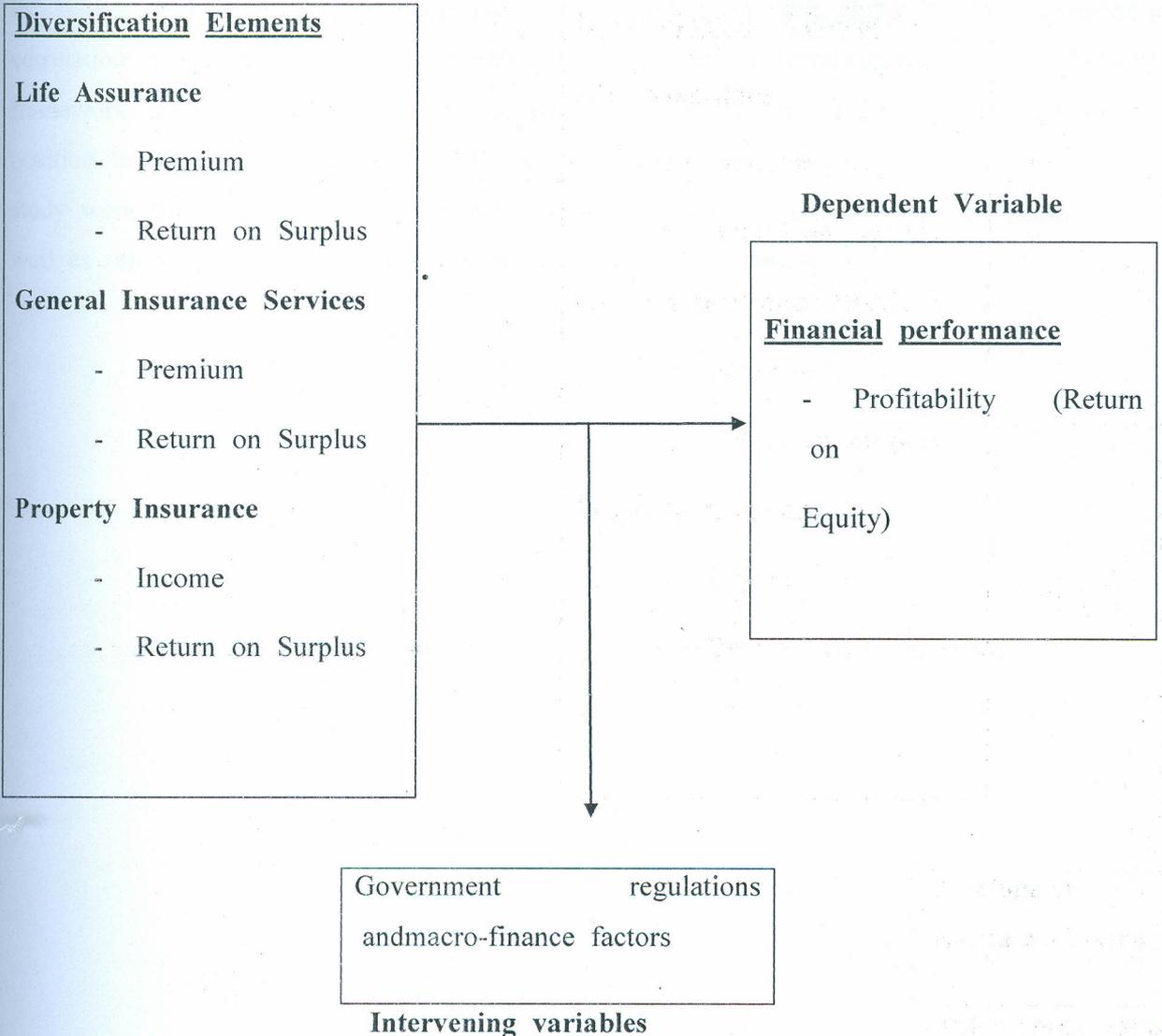


Figure 1.1: Relationship between Investment Diversification and Financial Performance Source: Yan (2010)

Figure 1.1 above shows that the financial performance of Old Mutual is affected by investment in the life assurance policy, general insurance policy and property insurance

policy. Indicators of performance under the insurance policies are premiums or income and return on surplus. The framework finally postulates the financial performance of the firm that was measured through profitability using return on equity (ROE). The theory that guided this study was the Modern Portfolio Theory (MPT) that Yan (2010) explains by stating that diversification improves firm profitability and there exists a positive correlation between the two variables. This helped in formulating the conceptual framework above. Other variables that were foreseen to might have also been in a position to affect the company's profitability but were not considered for this particular study were the government policies relevant to the industry and country of operation as well as other macro-economic factors such as social and demographic factors.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter is a review of the literature that will guide the researcher in achieving the study objectives. The chapter begins with theoretical reviews, empirical reviews and finally a summary of the reviewed literature.

2.2 Theoretical Review

2.2.1 Modern Portfolio Theory

The Modern Portfolio theory states that to reduce a portfolio risk, one can do so by simply holding combinations of instruments that are not perfectly positively correlated (West, 2006). Megginson (2003) cited that no matter the level of risk tolerance, investors in the market would always maintain stock portfolios. The portfolio theory has several assumptions which are also said to be the limitations of the theory. The assumptions are; investors are rational, investors have the same risk appetite, there is perfect information, unlimited access to capital and no taxes nor transaction costs (Veneeya, 2006). This theory is based on the idea that risk-averse investors can construct portfolio to optimize expected returns by minimizing risk (Bodie et.al 2009). A portfolio risk is measured using standard deviation (Amihund, 2002). Variables of risk generally include market fluctuations, competition, sources of financing and type of shareholders.

The ultimate objective of portfolio analysis is to determine the portfolio which provides the investor with the most suitable combination of risk and return (Markowitz, 1959). The diversification strategy can influence the investment appraisal process and the choosing of opportunities for investment. Furthermore, the type and range of investments expected returns influence the discounting process during the determination of present values. Therefore, this study variables relationship focuses on the principle of maximum return at minimum risk associated with diversification of investment opportunities. This theory is relevant to this study given that the Old Mutual engages in portfolio diversification including venturing in real estate, insurance services and fund management as a possible way of lowering the risk of loss from investments.

2.2.1.1 Diversification Concept

Klein, Crawford, and Alchian, (2011) states that diversification is pursued by firms for a number of reasons; it might be driven by increasing demands from managers and employees to diversify, to preserve organizational and reputational capital, or it can be sought for tax and financial advantages or for risk reduction. Diversification strives to ensure smooth and efficient transition of firms' knowledge to other business activities hence helping in the firms' continuity (Campa and Kedia, 2002). It is a major strategic decision for a firm to choose to diversify (Elango and Ma, 2003).

As much as diversification is considered as a key driver for the firms' growth and as a strategic decision, the cost of diversification as shown in studies by Vishny (2006) and Yost (2002) far outweighs the benefit of diversification. According to Ansoff, the forth strategy is diversification strategy and there are two dimensions of it which are market diversification and product diversification (Njoroge, 2003).

2.2.1.2 Product Diversification Concept

Johnson and Scholes (2002) define diversification as a strategy used by an organization to take it away from its current markets or products or even competencies. It addresses the strategic question of which product a firm should produce and which markets it should enter as well as how it should do so. Diversification, according to Maweu (2012) has two dimensions which are product diversification and market diversification. For a product diversification strategy to be considered the best, it should be one which reinforces the firm's existing resources and strengths as well as creating basis for new ones (Burgers et al., 2009).

Marangu (2013) states that Ansoff and McDonnell argue that the three reasons as to why firms might think to pursue product diversification are: when their objectives cannot be achieved by continuing to supply the already existing products, when the business environment has changed to threaten the future growth and present opportunities, when there appears to be better opportunities presented by engaging in new products and finally, when a business tends to have excess resources to spare for more investments.

revealed that investment diversification among banks in Ethiopia including investing in government security, loan portfolio, insurance, investment size and financial assets positively impacted on their financial performance.

Maina (2013) assessed how microfinance companies had their financial performance impacted by product diversification and the study indicated that diversification indicators, ROE and ROA indicators grew. Rop, Kibet, and Bokongo (2016) also conducted a study on how investment diversification impacted on the financial performance of Kenyan Commercial Banks. Their study adopted an exploratory research design to help determine the causal relationship between investment diversification and financial performance targeting 40 commercial banks in Kenya and the recommendation was that banks needed to focus on building confidence in and promoting diversification.

2.3.1 Investment in Life Assurance and Firm Performance

Mutugi (2012) sought to find out the factors that influence financial performance of life assurance companies in Kenya and his findings were innovation, ownership structure and diversification. The idea of insurance can be traced back to thousands of years. The insurance Principle of building reserves for the future is illustrated by the biblical story of Joseph and the famine in Egypt. The code of Hamurabi, the collection of Babylonian laws of the 1700 B.C included the form of credit insurance. Life assurance dates back to Raman times. The first successful insurance company, the amicable society for a perpetual assurance office was founded in England in 1705-1706 (Encyclopedia, 2018). Life assurance business was introduced into Ethiopia based on mutual assistances and its modern form traces back to 1905, when bank of Abyssinia began to offer the services.

2.3.2 Investment in General Insurance and Firm Performance

The profitability of general insurance policy is influenced by both internal and external factors (Adams and Buckle, 2000). Teece (2009) states that large companies can exploit economies of scale and scope; thus being efficient by providing general insurance policy amongst other policies. A key factor that can improve the financial performance of a company that offers general insurance is the age of the company which translates

to experience in the industry (Ahmed, Ahmed and Ahmed). Wabita (2013) also sought to find out determinants of financial performance of general insurance companies and established that growth in the industry which can be achieved through the grand strategies such as diversification is one of the key factors.

2.3.3 Investment in Property Insurance and Firm Performance

Most economic analysts and investors tend to focus on return on equity as their primary measure of a company performance (Hagel, Brown & Davison, 2010). The most significant trends in the insurance industry are prevalence of diversification, mergers and acquisitions. Konagai (2009) did a study on Japan REIT performance and established that performance could be seen as good once they are matured with a good history background. However, a study was conducted in Kenya by Michuki (2010) on real estate investment in Kenya and found contradicting results from other studies that the real estate illiquid nature increases transaction costs and might not actually result to an improved financial performance of a company.

2.4 Summary of the Literature Review

The reviewed literature has identified theories that explain the need for diversification for firms gearing towards improved financial performance. Further, evidence from empirical literature strongly reveals the positive impacts of diversification among firms. The previous studies reviewed majorly focused on the banking sector in a bid to assess the impact of investment diversification on financial performance of firms with some going into the details of the most effective types of diversification. These studies utilized different methodologies including multivariate and univariate study methodologies, quantitative research design and descriptive survey design. The current study sought to add knowledge to the research gaps that currently exist by assessing the influence of diversification on the performance of an investment firm. Further, the study utilized a quantitative and qualitative approach as the study design.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The philosophy of a research is a belief about the way in which data about a phenomenon should be gathered, analyzed and used. Two major research philosophies can be identified, namely positivist (sometimes called scientific) and interpretivism (anti-positivist) Hassan (2011). Positivists believe that reality is stable and can be observed and described from an objective viewpoint (Klein, 2003), without interfering with the phenomena being studied.

The beginning of designing a research is the specification of research paradigm after defining the topic of concern. Research paradigm is a broad view or perspective of a study (Taylor *et al.*, 2006) or patterns of beliefs and practices that regulate inquiry within a discipline by providing lenses, frames and processes through which investigation is accomplished (Weaver and Olson, 2006). Morgan (2007) advanced the importance of research paradigm. They highlighted its functions as those of defining how the world works, how knowledge is extracted from this world, and how one is to think, write, and talk about this knowledge and; defining the types of questions to be asked and the methodologies to be used in answering them. They also argued that a paradigm structures the world of the academic worker and; provides its meaning and its significance. This study was guided by quantitative positivism paradigm, since it is an inquiry based on testing of variables measured in numbers and was analyzed with statistical procedures, in order to determine whether the predictive generalizations of the theory held were true; this concurs with studies done by Cresswell (2003).

3.2 Research Design

The study adopted a correlation survey research design. According to Nachmias and Nachmias (2008), a survey design is most suitable in a research aimed at establishing a problem and determining its extent. The correlation approach helped to determine whether and to what degree a relationship exists between the quantifiable variables in

this study and this concurs with past scholarly works of Mugenda and Mugenda (2003) and Cooper and Schindler (2003).

3.3 Target Population

The target population of this study was investment firms. Investment firms are firms that are principally engaged in investing securities on behalf of the clients as well as offer other financial advice. Kenya has 52 investment firms according to yellow pages (<https://yellow.co.ke>, 2019) with 6 listed in the Nairobi Securities Exchange.

3.4 Sample Design

The study adopted a non-statistical sampling which is also known as purposive sampling and judgment sampling. It was the better option since the study population was below 100 units. This type of sampling design enables the researcher to make selection of a test group based on his/her judgment rather than formal statistical method. Through this design, the researcher could select the sample size, the items selected for the test group and how the results are evaluated.

The guide to choosing the sample size in this study was the number of products an investment company deals with, which was; what investment firm is highly diversified and the oldest formulated investment company. Also Market diversification would be taken into consideration, which was; which investment firm is listed in the most securities exchange markets.

Old Mutual is listed under 4 Stock Exchange markets, namely; Johannesburg Stock Exchange, Zimbabwe, Malawi, Namibia and London Stock Exchange. It is the oldest formed investment company which was established in 1845 in South Africa. Old Mutual has a diversified investment portfolio encompassing different insurance policies. Therefore, Old Mutual being the best fit in relation to the guide set above was used for the study.

3.5 Research Instrumentation

This study used secondary data. Secondary data was obtained from the Old Mutual financial records and was used in this study. The researcher obtained data on

performance indicators for life assurance policy, general insurance policy, property insurance policy and returns of the firm. The data obtained was for the period from 2014 to 2017.

3.5.1 Validity of the Research Instruments

The validity of the data collection instruments was done using experts in the finance field to clarify the ambiguity parts in order to improve on both content and validity of the instrument. Kimberlin & Winterstein (2008) observes that data validity is the measure of research instrument's accuracy when measuring variables of the study. Data validity is used to indicate whether the research instrument really measures what it purports to measure. The data collection guide will be subjected to thorough and logical evaluation process in order to ensure that the collected data is valid. This was done through peer and expert review of the financial statements.

3.6 Data Analysis and Presentation

The data collected was analyzed using descriptive and inferential statistics. Descriptive statistics was used to summarize and analyze the data, involving measures of dispersion and central tendency where means and averages and regression analysis. A regression analysis was also used to assess the relationship between the variables in this study (Marsh *et al.*, 2011). Content analysis was performed on qualitative data. Data was presented using tables, figures and charts. The analytical model used in this study was based on Kahloul and Hallara (2010) who researched on diversification, risk and performance relationship. The regression model below was adopted; $Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e_0$

Y = Financial performance of Old Mutual (Profitability)

X_1 = Life Assurance Policy

X_2 = General Insurance Policy

X_3 = Property Insurance Policy

B_0 = Regression constant

β_1, β_2 and β_3 = Coefficients associated with predictor variables

e_0 = Residual (error) term

CHAPTER FOUR

RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter highlights presentations and findings. The data was analyzed using descriptive and inferential statistics and the final discussion of the findings aligned to the specific study objectives. The inferential statistics that were used included linear regression models and correlation analysis so as to determine the strength of the relationships between the dependent and the independent variables presented in tables. Descriptive statistics which include the mean, standard deviation, minimum and maximum values of the variables were also captured in tables.

4.2 Information on Financial Performance of Old Mutual

This study sought to find out the financial performance of Old Mutual in relation to the portfolio it holds. This referred to information about the profitability of Old Mutual. It also referred to the portfolio mix or the investment diversification of Old Mutual which includes life assurance package, general insurance package and property insurance package with key performance indicators as premium, claims, return on surplus ratio which is the same as return on equity, income and expenses. This information was necessary as it formed the basis of the financial performance of Old Mutual in summary. The study findings are presented in table 4.1.

The study findings indicated that there has been an inconsistent trend on the profitability % change of Old Mutual from 2014 to 2017. There was an increase in percentage on profitability of Old Mutual from 13.3% in 2014 to 14.2% in 2015. Afterwards, there was a drop to 13.3% in 2016 and then an increase to 14.6% in 2017.

The net premium received from both life assurance and general insurance in totality increased from Shs. 11,263,533 in 2014 to Shs.15, 497,553 in 2017. The claims from both life assurance and general insurance in totality increased from Shs.8, 074,794 in 2014 to Shs. 7,986,649 in 2015 then decreased to Shs. 9,390,241 in 2017. The

inconsistency in trend replicates that for profitability in terms of the movement of figures.

Table 4.1: Data of Performance Indicators of Life Assurance

Year	Sub	LA-Net Premium	LA- Claim	GEN-Net Premium	GEN- Claim	PROP- Income	PROP- Expense	GEN- ROE
2017	Kenya	998,448	-1087687	8,188,615	-5039847	0	-0	14.6
2017	Uganda	981,384	-749111	2,014,513	-1071243	781,497	-115398	14.6
2017	Rwanda	0	-0	954,547	-673588	0	-0	14.6
2017	Tanzania	0	-0	988,134	-407018	0	-0	14.6
2017	S.Sudan	67,653	-20822	1,304,259	-340925	199,393	-147601	14.6
2016	Kenya	960,112	-1777182	8,453,260	-5836675	0	-0	13.3
2016	Uganda	714,705	-576009	1,891,268	-977897	442,873	-181596	13.3
2016	Rwanda	0	0	769,952	-548895	0	-0	13.3
2016	Tanzania	0	0	987,968	-473998	0	-0	13.3
2016	S.Sudan	84,774	-19348	1,564,997	-225959	143,720	-297110	13.3
2015	Kenya	873,183	-1035516	6,227,334	-4289962	0	-0	14.2
2015	Uganda	475,452	-952132	1,853,815	-952132	55,121	-78261	14.2
2015	Rwanda	0	-0	450,845	-379725	0	-0	14.2
2015	Tanzania	0	-0	977,743	-486671	0	-0	14.2
2015	S.Sudan	52,670	-20226	1,158,384	-495423	1,291,123	-127380	14.2
2014	Kenya	1,342,882	-2144673	6,063,039	-4100385	0	-0	13.3
2014	Uganda	314,786	-148523	1,710,070	-853975	867,766	-234219	13.3
2014	Rwanda	0	-0	213,370	-182130	0	-0	13.3
2014	Tanzania	0	-0	648,418	-265948	0	-0	13.3
2014	S.Sudan	12,194	-72577	958,774	-371902	309,099	-82588	13.3

The findings also indicated that Income from property insurance had a trend of decrement from Shs.1, 176,865 in 2014 to Shs.1, 346,244 in 2015 then Shs.586, 593 in

2016 and later increased to Shs. 980,890 in 2017. This trend also correlates with the profitability trend from the look of the movement of figures.

4.3 Descriptive Statistics of the Variables

A descriptive analysis of the data collected on the variables was assessed by the researcher for the purpose of understanding the distribution of the data collected. These included mean, standard deviation, minimum and maximum values of the variables. The findings are presented in table 4.2 below.

Table 4.2: Descriptive Statistics of Old Mutual Data
Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
LA-Net Premium	20	0.00	1342882.00	343912.15	454957.01
LA-Claim	20	-2000000.00	0.00	-430000.00	654500.00
GEN-Net Premium	20	213370.00	8453260.00	2368965.25	2588440.39
GEN-Claim	20	-6000000.00	-200000.00	-1400000.00	1799000.00
PROP-Income	20	0.00	1291123.00	204529.60	366292.73
PROP-Expenditure	20	-300000.00	0.00	-63200.00	91900.00
GEN-Return on Equity	20	13.30	14.60	13.85	0.58
Valid N (listwise)	20				

The findings presented in table 4.2 shows that the mean of premium of Old Mutual from life assurance policy was 343,912.15 with a standard deviation of 454,957.01. The mean of claim from life assurance was (430000.00) with a standard deviation of 654,500.00. The return on equity had a mean of 13.85 with a standard deviation of 0.58, a maximum of 14.60 and minimum of 13.30.

The findings also indicated the mean of premium from general insurance was 2368965.25 with a standard deviation of 2,588,440.39. The mean of claim from general

insurance was (1400000.00) with a standard deviation of 1799000.00. The mean of property insurance income was 204529.60 with a standard deviation of 366292.73, while the property insurance expenditure had a mean of (63200.00) and with standard deviation of 91900.00 according to table 4.2 above.

4.4 Inferential Statistical Analysis of Old Mutual Data

To be able to understand the relationship between the dependent variable and independent variables identified by this study, the researcher conducted inferential statistical analysis involving multiple linear regression analysis. This also proved essential in determining the significance of the coefficients of the explanatory variables. The fitness of regression model was also determined through the analysis of variance generated. This was followed by a correlation analysis used in establishing the direction of relationship that existed between the independent variable and the dependent variable.

4.4.1 Correlation Coefficient Analysis

This study used Pearson correlation coefficient which measures the strength of linear association between two variables. It is usually denoted by r and it takes any value in the range of +1 to -1. Correlation coefficients (r) of values greater than 0 imply positive associations, less than 0 imply a negative association, while 0 implies that there is no association at all between the two variables. The findings from the correlation analysis between the independent variable and the dependent variable are presented in table 4.3, 4.4 and 4.5 below.

Table 4.3: Correlation Coefficient Analysis

		LA-Net Premium	LA- Claim	GEN-Return on Equity
LA-Net Premium	Pearson Correlation	1	-.931**	.028**
	Sig. (2-tailed)		.000	.007
	N	20	20	20
LA-Claim	Pearson Correlation	-.931**	1	.070**
	Sig. (2-tailed)	.000		.003
	N	20	20	20
GEN-Return on Equity	Pearson Correlation	.028**	.070**	1
	Sig. (2-tailed)	.007	.003	
	N	20	20	20

** . Correlation is significant at the 0.01 level (2-tailed).

The study findings presented in table 4.3 above show that the net premium from life assurance policy has a strong negative relationship ($r = -0.931$) with the claim from life assurance policy having a significance of 0.000, meaning it is highly to occur since its significance level is lesser than 0.05 and a weak positive relationship ($r = 0.028$) with return on equity of Old Mutual with a higher significance level of 0.007.

The life assurance claims also had a weak positive relationship ($r = 0.070$) with the return on equity of Old Mutual with a significance value of 0.003, meaning its likelihood to occur is high since the significance level value is lesser than 0.05.

Table 4.4: Correlation Coefficient Analysis

		GEN-Net Premium	GEN- Claim	GEN-Return on Equity
GEN-Net Premium	Pearson Correlation	1	-.991**	.036**
	Sig. (2-tailed)		.000	.002
	N	20	20	20
GEN-Claim	Pearson Correlation	-.991**	1	-.018**
	Sig. (2-tailed)	.000		.004
	N	20	20	20
GEN-Return on Equity	Pearson Correlation	.036**	-.018**	1
	Sig. (2-tailed)	.002	.004	
	N	20	20	20

** . Correlation is significant at the 0.01 level (2-tailed).

The study findings presented in table 4.4 show that the net premium from general insurance has a strong negative relationship ($r = -0.991$) with the claim from general insurance with a high likelihood of occurrence ($p\text{-value} = 0.000$) while it has a weak positive relationship ($r = 0.036$) with the return on equity of old mutual with a likelihood of 0.002 occurrence showing higher confidence level. The general insurance claim on the other hand had a weak negative relationship ($r = -0.018$) with the return on equity of old mutual with a significance value of 0.004.

The findings presented in figure 4.5 below show that property insurance income had a weak positive relationship ($r = 0.058$) with return on equity of old mutual with a significance value of 0.007, its expenditure had a weak positive relationship ($r = 0.165$) with return on equity with a significance value of 0.006.

Table 4.5: Correlation Coefficient Analysis

		PROP- Income	PROP- Expenditure	GEN-Return on Equity
PROP-Income	Pearson Correlation	1	-.597**	.058**
	Sig. (2-tailed)		.005	.007
	N	20	20	20
PROP-Expenditure	Pearson Correlation	-.597**	1	.165**
	Sig. (2-tailed)	.005		.006
	N	20	20	20
GEN-Return on Equity	Pearson Correlation	.058**	.165**	1
	Sig. (2-tailed)	.007	.006	
	N	20	20	20

** . Correlation is significant at the 0.01 level (2-tailed).

4.4.2 Regression Analysis

This study developed an estimated regression analysis from the model developed in chapter three of the study. An analysis of the model is presented as follows:

4.4.2.1 Model Summary

The study carried out determination coefficient (R²) analysis to determine the proportion of variation in the dependent variable attributable to variations in the independent variables. This was presented in table 4.6

Table 4.6: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.77 ^a	.59	.4806	.4062

a. Predictors: (Constant), Property Insurance, Life Assurance, General Insurance

The R² for the model was 0.59, implying that only 59% changes in return on equity of old mutual was attributed to or can be explained by changes in life assurance, general insurance and property insurance and 48.06% when adjusted for degree of freedom

(adjusted R square = 0.4806). The prediction by the model is accurate at 40.62% (standard error of the estimate – 0.4062). R is the correlation between the observed and predicted values of dependent variable (0.08) indicating a strong positive correlation.

4.4.2.2. Analysis of Variance

ANOVA statistics were also relied on by the study to determine the overall significance of the regression model. This is presented in table 4.7 below. With the level of significance as 0.002 being greater than 0.05, there is evidence of a statically significant effect between the study variables.

Table 4.7: ANOVA^a

	Model	Sum of Squares	Df	Mean Square	F	Sig.
	Regression	3.8055	3	1.269	.035	.002 ^b
1	Residual	2.6445	16	.165		
	Total	6.450	19			

a. Dependent Variable: ROE

b. Predictors: (Constant), Property Insurance, Life Assurance, General Insurance

4.4.2.3 Model Coefficients

Table 4.8 shows the regression coefficients of the independent variables that affect the profitability of Old Mutual.

With the model being specified as:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \dots + \beta_n X_n + e_0$$

The estimated model based on the analysis presented in table 4.8 therefore would become:

$$\text{Financial performance of Old Mutual} = 13.778 - 0.06705X_1 + 0.02119X_2 + 0.01233X_3 + e_0$$

Where:

Y = Financial performance of Old Mutual (Return on Equity of Old Mutual).

X₁, X₂ and X₃=Independent variables (Premium from life assurance policy, premium from general insurance policy and income from property insurance).

β_0 - a constant

$\beta_1, \beta_2, \beta_3 \dots \beta_n$ = Coefficients of the independent variables

e_0 = Error term

Table 4.8: Regression coefficients of the model

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	13.798	.226		61.113	.000
Life Assurance	-0.6705	6.095	-.052	-.110	.000
General Insurance	0.2119	1.09	.094	.194	.001
Property Insurance	0.1233	0.4281	.077	.288	.003

a. Dependent Variable: Return on Equity

4.5 Discussion of findings based on study objectives

4.5.1 Effects of life assurance policy on financial performance of Old Mutual

Objective one sought to determine the effect of life assurance policy on financial performance of Old Mutual. A null hypothesis was developed stating that there is no relationship between life assurance policy and financial performance of Old Mutual. The results as presented in table 4.8 above gives net premium from life assurance-value of 0.007, r of 0.028 and r^2 of 0.0%.

This indicates a positive correlation between life assurance and financial performance of Old Mutual. It means, therefore, that net premium from life assurance policy affects only 0.0% of financial performance of Old Mutual. The null hypothesis is rejected in this case since net premium from life assurance policy has p-value lesser than 0.05.

West (2006) in his study found out that diversification and financial performance were not perfectly correlated. This study however disagrees with that finding since in this

study diversification has been proofed to be correlated with financial performance of Old Mutual. Life assurance policy has a positive correlation with the financial performance of Old Mutual. Also, the correlation of dependent variable and the independent variables was established to be a perfect positive correlation. This study therefore agrees with Megginson (2003) that no matter the risk tolerance level, a stock portfolio should be maintained for better financial performance and Johnson & Scholes (2002) that diversification can lead to a better financial performance by giving a firm its competitive advantage.

4.5.2 Effects of general insurance on financial performance of Old Mutual

Objective two sought to determine the influence of general insurance policy on financial performance of Old Mutual. A null hypothesis was developed stating that there is no relationship between general insurance policy and financial performance of Old Mutual. The results as presented in table 4.8 above gives net premium from general insurance a p-value of 0.002, r of 0.036 and r^2 of 0.1%.

This indicates a positive correlation between net premium from general insurance and financial performance of Old Mutual. It means, therefore, that net premium from life assurance policy affects only 0.1% of financial performance of Old Mutual. The null hypothesis is hence rejected in this case since net premium from general insurance policy has p-value lesser than 0.05.

This study concurs with Marangu (2013) that one reason as to why a portfolio should be held is when a business environment has changed. The current business environment has changed and every person takes insurance as a risk mitigation strategy. Old Mutual is better placed to fit in to this changing business environment by also offering general insurance on top of the other services it offers. This study however disagrees with Kahloul & Hallara (2010) that diversification and profitability of a firm lacks a linear relationship because as seen in the findings, there is a linear relationship between the independent and the dependent variables. With a positive linear relationship that this study established between diversification and profitability of Old Mutual, this study concurs with Chen & Yu (2011).

4.5.3 Effects of property insurance on financial performance of Old Mutual

Objective three sought to determine the impact of property insurance policy on financial performance of Old Mutual. A null hypothesis was developed stating that there is no relationship between property insurance policy and financial performance of Old Mutual. The results as presented in table 4.8 above gives income from property insurance a p-value of 0.007, r of 0.058 and r^2 of 0.3%.

This indicates a positive correlation between property insurance and financial performance of Old Mutual. It means, therefore, that income from property insurance policy affects only 0.3% of financial performance of Old Mutual.

The null hypothesis is rejected in this case since income from property insurance policy has p-value lesser than 0.05.

Rop, Kibet & Bakongo (2016) established a positive correlation between diversification and financial performance in agreement with Rotich et al (2016). This study also agrees with the mentioned studies that the positive correlation exists between diversification and financial performance of a firm. Michuki (2010) however disagrees with the above findings in his study conducted on real estate industry that concluded that there exists a negative correlation between diversification and financial performance of firms measured through profitability. Marangu (2013) further states that one reason for holding a portfolio is that better opportunities are presented by engaging in new products. Old Mutual is therefore at an advantageous position by engaging in property insurance services as its product.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This chapter presents the summary of findings of the study, conclusion, recommendations and suggestions for further research based on the findings.

5.2 Summary of findings

The study found that portfolio diversification had an implication on financial performance of Old Mutual, which means that when investment firms' portfolio become more diversified the financial performance, is likely to increase. A positive correlation between the key performance indicators of the financial

5.2.1 Effect of life assurance policy on financial performance of Old Mutual

Investment in life assurance policy has a correlation on the financial profitability of Old Mutual. The net premium from this policy had a weak positive relationship with the general return on equity of Old Mutual. This shows that life assurance has an impact on Old Mutual financial performance with regards to its profitability measured as return on equity but of a small percentage. In relation to the first hypothesis, the study proved that there indeed is a relationship between life assurance policy and the financial performance of Old Mutual, though a weak positive relationship.

5.2.2 Effect of general insurance policy on financial performance of Old Mutual

General insurance policy has a correlation with the profitability of Old Mutual. The net premium from this policy had a weak positive relationship with the general return on equity of Old Mutual. Meaning investment in general insurance policy influences the profitability of Old Mutual. This shows that general insurance has an impact on financial performance of Old Mutual with regards to profitability measured as return on equity. In relation to the second hypothesis, the findings of the study proved that there exists a weak positive relationship between general insurance policy and financial performance of Old Mutual.

5.2.3 Effect of property insurance on financial performance of Old Mutual

Investment in property insurance policy has a relationship with the financial performance of Old Mutual. The net premium from this policy had a weak positive relationship with the general return on equity of Old Mutual. Meaning the premium from this policy affects a small portion of the profitability of Old Mutual. The claims of this policy had a weak positive relationship with the general return on equity. Meaning, it also influences the profitability but just a small fraction of it. This shows that property insurance has an impact on the financial performance of Old Mutual as it affects a portion of its profitability measured using return on equity. In relation to the third hypothesis, the study findings reflected that there exists a weak positive relationship between property insurance and the financial performance of Old Mutual.

5.3 Conclusion

The study findings concluded that investment in life assurance policy by Old Mutual had statistically significant influence on the profitability of Old Mutual. The findings, revealed a positive correlation between the premium from this policy and profitability of Old Mutual. Meaning, an increase in premium from life assurance policy would lead to an increase in profitability of Old Mutual and the opposite is true.

General insurance also had statistically significant influence on profitability of Old Mutual. There was revealed to be a positive relationship from the correlation analysis between the net premium from this policy and the profitability of Old Mutual, however there was an inverse relationship from the correlation analysis between the claims on this policy and the profitability of Old Mutual. Meaning, an increase in the premium from this policy would automatically lead to an increase in profitability of Old Mutual while an increase in claims on this policy does not mean an increase in profitability of the firm.

Property insurance policy was also revealed to have statistically significant impact on profitability of Old Mutual. A correlation analysis of income from this policy and profitability of Old Mutual was actually witnessed to be a positive one. Meaning, there exists a positive correlation between the income from this policy and profitability of

Old Mutual (an increase in the income would lead to an increase in profitability and the opposite is true).

5.4 Recommendation

Based on objective one which sought to establish the effect of life assurance policy on the profitability of Old Mutual, since the study found out that the policy has a positive correlation with the profitability of Old Mutual, the study recommends that the firm should continue offering this policy as one of its insurance packages and work to ensure that the claims from this policy maintains the relation it has with the premium (negative correlation). This is so that profit is realized from higher premium in relation to claims.

Objective two sought to find out the influence of general insurance policy on the financial performance of Old Mutual and the policy was established to be having a strong positive correlation with the profitability of the firm. The study therefore recommends that Old Mutual should continue investing also in this policy as its positive performance would translate to an increase in the firm's profitability.

In relation to the third objective, the study recommends that Old Mutual should continue offering the property insurance policy too as it has a positive correlation with the profitability of the firm. The firm should promote this policy so that it can have increased income from it to boost its profitability. This study also recommends that management should opt for cost effective strategies for more significant positive relationship between diversification and financial performance. It would be profitable to adopt these strategies and probably consider other strategies only when their costs are low because investment gains may be small relatively to business size.

In conclusion, the study recommends that investment firms and other firms that offer insurance services should encourage diversification into more insurance policies. This is because as seen in this study, every policy studied above has a positive relationship with the profitability of the firm. Therefore, it might be a good thing for a firm to increase its diversification of the policies.

Further research should be conducted on how diversification compares to other grand strategies like mergers and acquisition in influencing a firm's financial performance more so in terms of profitability.

5.5 Limitations of the study

This study was limited to secondary data. The financial statements were utilized to gather the required data since Old Mutual has its headquarters in South Africa and getting primary data of what affects its financial performance would not have been possible. The study was conducted solely on Old Mutual relying on its audited financial reports.

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