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EFFECT OF RISK TRANSFER STRATEGY ON THE PERFORMANCE OF SELECTED INSURANCE COMPANIES IN NAIROBI CITY COUNTY, KENYA

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Abstract: **The insurance sector is crucial in offering new ideas to address significant societal, financial, and ecological issues confronting the country. Even though the insurance sector plays a significant role in the economy of Kenya, the level of insurance coverage in the country is still minimal. The recent epidemic has impacted the insurance industry's performance, leading to losses for most companies and ongoing customer complaints. Therefore, the study sought to establish the effect of risk transfer strategy on the performance of selected insurance companies in Nairobi County, Kenya. This research utilized a descriptive research methodology. This study focused on 10 chosen insurance companies in Kenya as its target group. 856 employees from the risk management and compliance departments of the chosen insurance companies were the participants. Survey participants were grouped based on the companies they belong to. Participants were chosen from each group through the use of basic random sampling methods. The sample consists of 273 employees. Primary data was gathered using a partially structured questionnaire. An initial study with 28 participants was conducted. The research utilized content validity, criterion validity, and face validity to assess the specific connection between the assessment and its targeted measurement. A Cronbach's alpha analysis was conducted to assess the consistency of the Likert scale multiple choice questions. The research utilized both qualitative and quantitative data. Thematic analysis techniques were utilized to examine the qualitative data gathered from the open-ended inquiries. Quantitative data was analyzed using descriptive statistical methods like mean and standard deviation. The research carried out statistical analysis, such as correlation and regression, to assess the level of relationship among the variables. The research discovered that the implementation of a risk transfer strategy had a notable and beneficial impact on the overall performance of specific insurance companies operating within Nairobi County, Kenya. The research concludes that risk transfer aids insurance companies in lowering financial and operational risks, enhancing efficiency and productivity, boosting flexibility and adaptability, and fortifying relationships with partners or suppliers. The research suggests that insurance companies should thoroughly investigate and conduct background checks on partners or suppliers before forming any agreements.**

Keywords: **Risk Management, Risk Transfer Strategy, Organizational Performance.**

1. INTRODUCTION

Determining business success or failure hinges on organizational performance, aiding in pinpointing problem areas, improving operations, assessing key success factors, evaluating other departments, managing performance, processes, and employee well-being (Rasid, Isa & Ismail, 2019). Pojasek (2020) noticed that organizations can decrease unforeseen and expensive emergencies and distribute resources more effectively by incorporating risk, enhancing communication, and enhancing organizational performance through outlining potential threats.

Part of the work life of individuals and organizations involves risks that are linked to potential events or situations that may jeopardize the attainment of organizational goals and objectives (Susanto & Meiryani, 2018). Frame (2020) notes that risk management plays a crucial role in predicting rapid environmental changes, enhancing corporate governance, improving strategic management, protecting organizational resources and assets, and minimizing reactive decision-making by top management. Hence, a thorough comprehension of risk management enables the company's management to efficiently address uncertainties involving risks and opportunities, ultimately improving the organization's capacity to deliver increased value.

Rochette (2019) notes that incorporating risk identification and management into a robust management and governance framework is essential. They recommend aligning risk management and performance measurement to help organizations define their risk profile and strategic direction effectively. Rogers, Lukens, Lin, and Jon (2017) suggest that organizations need to actively address risks in order to bridge performance gaps. It is important for organizations to recognize that a strategy without alignment with risk management is not just inadequate, but also perilous. Thus, implementing a strategy in a reckless and unbalanced manner can significantly harm a company's performance.

The ongoing presence of risks and their impacts in the insurance sector led to the establishment of regulatory agencies to monitor insurance companies and develop strategies and rules to help manage these risks. For example, Batool and Sahi (2019) note that the National Association of Insurance Commissioners (NAIC) was founded in the US to provide standard-setting and regulatory assistance to every state. Nevertheless, insurance companies have been experiencing underwriting losses, reduced premiums, and an overall decrease in net income. In Europe, Ruiter (2021) notes that the European Insurance and Occupational Pension Authority (EIOPA) has the responsibility of enhancing a solid regulatory framework and overseeing the insurance sector. Nevertheless, the insurance industry has suffered from poor investment returns due to the prolonged low interest rate environment.

The main role of an insurance company is to handle risk. Nevertheless, many insurance firms in Nigeria typically handle risks in a conventional, compartmentalized way rather than a comprehensive approach (Onyeka, 2017). Ayeleso (2018) notes that NAICOM released the 'Guidelines for developing risk management framework for insurers and reinsurers in Nigeria' in 2012, mandating all insurance companies to create a system for identifying, evaluating, controlling, minimizing, and overseeing significant risks based on the company's risk management principles, beliefs, attitudes, values, culture, and operational approach.

Kiptoo, Kariuki and Ocharo (2018) stated that the growing risks and challenges in Kenya's insurance industry led the Insurance Regulatory Authority (IRA) to create a detailed risk management guideline for the sector. The guideline pinpointed credit risks, liquidity risk, market risk, and operational risk as among the different risks that must be controlled by an insurance company. Recently, it has been noted by Obudho (2019) that risk management is now seen as crucial across all sectors of the economy, in order for organizations to safeguard their interests while working towards their objectives. By managing risks, organizations can guarantee their desired outcomes, minimize the effects of threats to acceptable levels, and enhance opportunities to capitalize and optimize benefits further.

A Risk Management strategy is a comprehensive method used to manage risks related to business activities. It involves using a practical framework of methods and processes to monitor and address events or situations that may impact the company's objectives at both a company-wide and organizational level (McShane, Nair and Rustambekov, 2019). Woods (2020) notes that organizational risk management strategies primarily aim to facilitate strategic and informed decision-making and offer a scalable and efficient method for addressing risks and opportunities across the entire enterprise.

Risk transfer strategy involves distributing risks with the help of external parties and can happen between organizations and insurance providers, insurance providers and policyholders, and insurance providers and reinsurance companies (Njegomir & Maksimovic, 2019). Thuku and Muchemi (2021) suggest that risk transfer strategies encompass utilizing insurance derivatives to shift risks from insurance companies to capital market investors, reinsurance where insurers transfer their risks to reinsurance companies, multiple insurance coverages merging to cover extremely high risks in a single contract, and group life insurance that provides coverage for a cohesive group under one contract. Hence, the shifting of risks helps insurance firms broaden their risk coverage, cut down on capital expenses, and ultimately increase the accessibility of insurance.

The Insurance Regulatory Authority (IRA) oversees the insurance industry in accordance with the Insurance Act Chapter 487 of Kenyan legislation. IRA is a governmental organization tasked with overseeing and supporting the development of the insurance industry in Kenya. In 1987, the Association of Kenyan Insurers (AKI) was established by Kenyan insurers with the primary goal of promoting ethical behavior among its members, raising public awareness, and advancing the insurance industry. In 2020, there were 56 insurance companies, up from 54 in 2019, while the number of reinsurance companies stayed constant at 5 in 2020. In 2020, the number of reinsurance brokers in the market increased by 2, reaching a total of 18. The number of insurance agents rose from 9,262 to 11,138. In 2020, there were 204 licensed insurance brokers in the market, which is 9 less than in the previous year.

The assets of the Kenya Insurance industry increased by 2.1 per cent to Kshs181.2 billion ($2.132 billion). There was a 33.1 per cent increase in net premiums to Kshs85.4 billion ($1.005 billion) and a 30 per cent rise in general insurance claims to Kshs28.1 billion ($330.6 million). As per the 2011 changes to the Insurance Act, an insurance company seeking to establish a new branch or location in Kenya, or to relocate an existing branch or place of business, must request approval from the Authority. The IRA currently considers insurer directors to be collectively and individually responsible for recovering assets in cases of mismanagement. The Authority was also granted the authority to oversee the assets of an insurance company for the benefit of the public and to take any necessary actions in relation to this matter (AKI, 2020).

2. STATEMENT OF THE PROBLEM

The Insurance Regulatory Authority (IRA) oversees the insurance sector in Kenya. The insurance sector plays a crucial part in offering inventive answers to the country's major social, economic, and environmental issues. In spite of the insurance sector's impact on the Kenyan economy, insurance penetration in Kenya stands at 2.73%, which is lower than the global average of 6.28%. The insurance industry in Kenya is currently facing numerous challenges, including the impact of the COVID-19 pandemic. This crisis has led to a drop in investment income from capital markets, lower premiums, and higher claims in certain insurance categories like medical. In order to lessen the effects of COVID-19, IRA provided insurance companies with some guidance notes. Nevertheless, customer grievances towards the insurance companies continue. Furthermore, a few insurance companies have been experiencing financial difficulties, leading to losses, closure, or being placed under statutory management because they are unable to meet customer claims.

3. LITERATURE REVIEW

Theoretical Literature Review

Portfolio Theory

In the 1950s, economist Harry Markowitz developed the portfolio theory, which emphasizes the importance of portfolios, risk, diversification, and the interconnections among different securities. The portfolio theory of investing aims to optimize portfolio expected return by choosing the right mix of proportions, either by reducing risk for a specific level of expected return or maximizing return for a given amount of risk. Markowitz (1952) asserts that investors can create a perfect portfolio for achieving maximum returns by balancing risk and choosing the ideal mix based on their individual risk tolerance.

Mangram (2013) noted that the Portfolio theory is a helpful instrument for selecting investments that will maximize total returns while managing a moderate level of risk. Diversification is highlighted as a crucial aspect in the portfolio theory. Most investments are either high-risk, high-reward or low-risk, low-reward. Ritchie and Bridley (2005) state that portfolio theory is a mathematical representation of the concept of investment diversification, aiming to select a set of investments that collectively carry less risk than any single investment. Hence, by merging both forms of investments, it can lead to a reduced total risk compared to doing them individually. However, diversification still decreases risk whether the investment returns are positively correlated or not negatively correlated. The theory is important in research because it shows how an organization can gain advantages from diversification through implementing multiple strategies, one of which includes reducing the risk of the portfolio.

Empirical Literature Review

Sibindi (2019) conducted a comparative analysis that examined the use of alternative risk transfer techniques in the insurance industries in Zimbabwe and South Africa. The research strategy employed was a longitudinal one, involving an analytical survey over a 10-year period from 2000 to 2010, with a focus on short-term insurance providers. Policyholders, brokers, and reinsurance companies made up the population. There was a use of both stratified random sampling and

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judgmental sampling. For the study, data from primary and secondary sources were collected. With the use of descriptive statistics, data were examined. The results of the study show that, in contrast to Zimbabwe, where the alternative risk transfer market is still in its infancy, South Africa has a fully developed market.

The study conducted by Biira, Tukei, Tukei, and Mboma (2021) investigated the correlation between Total Uganda Limited's performance and its risk transfer strategy. Both quantitative and qualitative methods were used to collect data for the study, which had a descriptive study design. 126 respondents provided the data, which was gathered via questionnaires. Qualitative data was gathered through key informant interviews. Correlation and regression analysis were utilized for the quantitative data, while content analysis was employed to examine the qualitative data. Results indicated that risk transfer strategies had a major impact on organizational performance.

Thuku and Muchemi (2021) examined how the performance of Insurance Companies in Nyeri County, Kenya is impacted by the risk transfer strategy employed. The research sample consisted of 66 managers from 22 insurance firms who play a direct role in risk management. Two kinds of research methodologies were employed: descriptive and explanatory. Self-administered questionnaires were utilized to collect primary data. The data was analyzed using the method of descriptive analysis. The research discovered that the risk transfer tactic greatly benefitted insurance companies' performance in Nyeri County.

4. RESEARCH METHODOLOGY

This research utilized a descriptive research methodology. This study focused on 10 chosen insurance companies in Kenya as its target group. 856 employees from the risk management and compliance departments of the chosen insurance companies were the participants. Survey participants were grouped based on the companies they belong to. Participants were chosen from each group through the use of basic random sampling methods. The sample consists of 273 employees. Primary data was gathered using a partially structured questionnaire. An initial study with 28 participants was conducted. The research utilized content validity, criterion validity, and face validity to assess the specific connection between the assessment and its targeted measurement. A Cronbach's alpha analysis was conducted to assess the consistency of the Likert scale multiple choice questions. The research utilized both qualitative and quantitative data. Thematic analysis techniques were utilized to examine the qualitative data gathered from the open-ended inquiries. Quantitative data was analyzed using descriptive statistical methods like mean and standard deviation. The research carried out statistical analysis, such as correlation and regression, to assess the level of relationship among the variables.

5. FINDINGS

The descriptive statistics results on risk transfer strategy are presented in Table 1.

Table 1: Risk Transfer Strategy

Statement	M	SD
Insurance companies enter into contractual agreements that clearly define the terms to minimize liability.	4.55	0.446
Insurance companies ensure that all aspects of their business operations are clearly outlined to reduce the potential for confusion or unmet expectations.	4.09	0.910
Utilizing subcontracting has helped companies mitigate the risks associated with hiring staff.	3.84	1.156
Subcontracting services have allowed companies to invest in specialized expertise.	3.57	1.430
The transfer of risk enables companies to cover financial losses up to the extent of policy coverage.	4.52	0.479
Implementing a risk transfer strategy has safeguarded insurance companies against unforeseen future risks.	4.49	0.509
Aggregate mean and standard deviation	**4.18**	**0.821**

The data presented in Table 1 demonstrates that the participants agreed on the impact of risk transfer strategy on the performance of specific insurance firms in Nairobi County, Kenya. This is supported by an average score of 4.18 and a standard deviation of 0.821. The participants were in strong agreement regarding the statements that insurance companies enter into contractual agreements that precisely define the terms of the agreement to reduce liability (M=4.55, SD=0.446)

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and that the transfer of risk has allowed the companies to mitigate financial losses up to the limit of policy coverage (M=4.52, SD=0.479). This indicates that by shifting the risk to a reinsurer, the primary insurer can restrict its vulnerability to catastrophic events that may lead to insolvency.

The participants reached an agreement on the following statements: Firstly, the implementation of a risk transfer strategy has effectively protected insurance companies from unforeseen future risks (M=4.49, SD=0.509). Secondly, insurance companies ensure that all aspects of their business operations are clearly defined in order to minimize confusion and prevent unmet expectations (M=4.09, SD=0.910). Thirdly, subcontracting has proven to be an effective method for reducing the risks associated with hiring staff (M=3.84, SD=1.156). Lastly, subcontracting services have allowed companies to invest in highly skilled expertise (M=3.57, SD=1.430). These findings suggest that the risk transfer strategies employed by insurance companies have the potential to meet their future expectations.

Inferential Statistics Results

Table 2: Correlation Analysis

		Risk transfer strategy	Performance
Risk transfer strategy	Pearson Correlation	1	
	Sig. (2-tailed)		
	N	270	
Performance	Pearson Correlation	.831	1
	Sig. (2-tailed)	.000	
	N	270	270

The correlation coefficient for the risk transfer strategy was 0.831, with a significance level of 0.00. This indicates a significant link between the risk transfer method and the operational results of specific insurance firms in Nairobi County, Kenya. This shows that the risk transfer plan has a significant association with the performance of certain insurance firms in Nairobi County, Kenya.

Regression Analysis Results

Table 3: Model Summary

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.778	.853	.834	0.281

The findings in Table 3 revealed that the adjusted R-square value stood at 0.834 (83.4%), demonstrating the impact of risk transfer strategy on performance. Hence, it can be inferred that the remaining 16.6% may be attributed to unexamined factors.

Table 4: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	202.153	1	202.153	771.576	.000
	Residual	70.124	268	.262		
	Total	272.277	269			

The results shown in Table 4 indicate that the p-value was 0.000, falling below the expected significance level of 0.05. The findings also show that the F value of 190.985 exceeds the mean square value of 50.538. The justification of these requirements validates the model's significance.

Table 5: Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.510	.118		4.322	.000
Risk transfer strategy	.771	.236	1.285	3.267	.001

The performance of selected insurance companies in Nairobi County, Kenya would be 0.510 (51.0%) when the risk transfer strategy is held constant, as shown in Table 5. An incremental rise in risk transfer strategy would boost the performance of chosen insurance firms in Nairobi County, Kenya by 77.1%. The research also found that the risk transfer strategy positively and significantly impacted the performance of chosen insurance firms in Nairobi County, Kenya ($\beta = 1.285$, $p < 0.05$).

The final regression equation is presented as follows:

$Y = 0.510 + 0.771X_1$

6. CONCLUSIONS

The research findings indicate that risk transfer assists insurance firms in diminishing financial and operational risks, enhancing efficiency and productivity, boosting flexibility and adaptability, and reinforcing relationships with partners or suppliers. This company can delegate non-core activities or tasks that are not its strength or priority to another party able to better absorb risks or offer compensation. The strategy of transferring risk also allows companies to utilize the expertise, information, and resources of their partners or suppliers while dividing both the risks and rewards of their efforts. Using a risk transfer strategy in risk management can help organizations enhance their resilience, safeguard assets, and enhance performance in a volatile business environment.

7. RECOMMENDATIONS

The research suggests that insurance companies should perform thorough investigations and screening of partners or suppliers prior to engaging in any agreements. The insurance companies need to set clear and achievable goals for the agreement, and also ensure they have consistent and open communication and feedback with partners or suppliers. The insurance companies need to regularly review and update the risk transfer agreement to align with any shifts in the risk landscape or the requirements and preferences of the parties involved.

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