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COST LEADERSHIP STRATEGY AND PERFORMANCE OF LIFE ASSURANCE COMPANIES IN KENYA

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ABSTRACT

The life assurance sector in Kenya has been striving to improve its performance in order to improve the overall livelihood of Kenyans. This study was conducted with the objective of investigating the effects of Cost leadership strategy on performance of life assurance companies in Kenya. The study adapted a descriptive research design. The target population was the 26 life assurance companies in Kenya consisting of 780 managers and unit of analysis was top, middle and line managers of all the 26 life assurance companies. Through systematic random sampling, a sample of 150 managers was selected. Primary data was collected using structured questionnaires with both open-ended and closed-ended questions. Reliability was tested through cronbach's alpha and research questionnaires were carefully checked to ensure they measured the content they were supposed to measure. The analysis of quantitative data was carried out using descriptive statistics which included frequencies, measures of central tendencies (mean) and measures of dispersion (standard deviation), correlation and regression model. The analysis was guided by use of statistical package for social sciences (SPSS version 23). The results revealed that cost leadership has a positive effect on performance of life assurance companies in Kenya. The study recommends that life assurance companies should sustain and continually improve on cost leadership strategy.

Key Words: Cost Leadership strategy, performance, Strategic Management, Life Assurance Companies

LIST OF ABBREVIATIONS

AKI- Association of Kenya insurers
BSC- Balance Score Card
CLS- Cost leadership strategy
EQ-Equity
IRA- Insurance Regulatory Authority
ICT - Information Communication Technology
OL - Organizational learning
PLAC- Performance of life assurance companies
PAT- Profit after Tax
RBV - Resource Based View
SPSS- Statistical Package for Social Sciences
SWOT- Strength Weakness Opportunity Threats
U.S- United States
UK- United Kingdom

1. INTRODUCTION

1.1 Background of the Study

Consistent high performance is one of the most important objectives in any company and is therefore one of the most important area, firms concentrates on. It is only through performance, firms are able to grow and progress. To ensure high performance, survival and success, firms need to develop capability to manage threats, exploit emerging opportunities and gain sustainable competitive advantage (Bennete, 2013). This involves creating competitive strategies that describes how a firm pursues competitive advantage across its chosen market scope (Porter, 1980). Competitive advantage can be attained if the current strategy is value-creating, and not currently being implemented by present or possible future competitors. Strategy is a set of action of a firm to achieve its goals and objectives (Thompson & Strickland, 2010).

Strategy represents a managerial commitment to pursue a particular set of actions in growing the business, attracting and pleasing customers, competing successfully, conducting operations and improving the company's financial performance. It enables the organization to maintain a sustainable competitive advantage; this is a competitive advantage that lasts longer period. An organization maintains a sustainable competitive advantage due to the incapability of the competitors to duplicate the firm's strategy, or finds the strategies costly to initiate, (Barney, 2010).

A company exists in turbulent and rapidly changing environments characterized by uncertainty and inability to predict the future, therefore management's major focus is on adjusting the organization according to the changing needs of the environment. A competitive strategy sets the long term plan of a particular company in order to gain competitive advantage over its competitors in the industry, (Kotler, 2011). They aim at creating defensive position in an industry, generating superior profits, maintaining a high market share and gaining customer loyalty which all lead to high performance in the organization. The drive to superior performance in a company is sustainable competitive advantage brought about by the competitive strategy used by the firm.

Porter (1980) described competitive strategies as strategies aiming to search for a strong position in the industry the organization is in. The competitive strategy is cost leadership; a firm sets out to become a low cost producer in its industry. It includes the pursuit of economies of scale, low manufacturing cost, preferential access to raw materials and other factors, (Daniella,2014). Cost leadership focuses on gaining competitive advantage by having the lowest cost in the industry, (Porter, 1996), this leads to high performance.

1.2 Statement of the Problem

Although life assurance has registered a constant growth from the year 2000 to 2010, the growth in the segment has declined significantly from 29.4% in 2014, to 8.6% in 2015 (AKI, 2015). AKI reports further shows that insurance penetration has declined from 2.93% of gross domestic product (GDP) in 2014, to 2.79% in 2015, compared to other developed countries, where penetration was 7.2% in 2015 in the U.S. Life assurance demand by the average Kenyan citizen is still low. Cost leadership is vital for any organization that concentrates on its performance.

Studies that have been done in this area include, strategies applied by health insurance companies to improve profitability (Boniface, 2011), strategies that influence the uptake of life assurance in Kenya (Kiumbi, 2011), effects of strategies adopted by insurance companies to attract business through agents (Stephen, 2013). There is therefore a need and a gap to carry out a research on the life assurance sector that will focus on cost leadership and performance of life assurance companies. With life assurance growth and penetration dropping, for any life assurance company to survive, it is important that it develops a good competitive strategy such as cost leadership that is crucial to achieve the organizations goals and objectives. Life assurance companies in Kenya are operating in an ever changing environment, in which new players continue to enter the market. Based on the above premise, this study seeks to investigate the effects of cost leadership and performance of life assurance companies in Kenya.

1.3 Objective of the Study

The objective was to determine the effect of cost leadership on performance of life assurance companies in Kenya.

1.4 Research Question

1. What is the effect of cost leadership strategy on performance of life assurance companies in Kenya?

1.5 Significance of the Study

This study will be of help to several parties; The Management of life assurance companies in Kenya; This study will benefit the management of life assurance companies in Kenya in that it will enable a proper evaluation of the present strategies, and identify their strengths and weaknesses, this will enable management in decisions of maintaining the strategies, and creating more that will improve the performance of the companies. It will provide opportunity to these life assurance providers to invest on more research and development. This study will benefit other researchers in that, the findings of this study will be used as reference in their research on related issues. It will also serve as a guideline to other researchers on issues related with cost leadership strategy in life assurance companies. This study will enable potential investors, policy holders and the public at large to understand and appreciate the challenges and opportunities in the life assurance industry. It will also clarify some of the issues misunderstood by people.

1.6 Limitation of the Study

Respondents were reluctant to fill in questionnaires since they considered information on their company performance sensitive. This would have led to inaccurate data and hence wrong conclusions from the study. To minimize the effect the researcher assured the respondents of confidentiality in handling the data they gave and assured them that the results were to be used for academic purpose only.

1.7 Scope of the Study

The study mainly focused on the staff of the 26 life assurance companies in Kenya which includes; top managers, middle level managers and lower level managers and it was be carried out in the life assurance companies' head offices. Descriptive research methodology was adapted in the study. The study focused on financial and non-financial performance data from 2012 to 2016.

2. LITERATURE REVIEW

2.1 Cost Leadership and Performance

Porter's generic competitive strategies state that in cost leadership, a firm sets out to become a low cost producer in its industry. It includes the pursuit of economies of scale, low manufacturing cost, preferential access to raw materials and other factors, (Daniella,2014). Cost leadership focuses on gaining competitive advantage by having the lowest cost in the industry, (Porter, 1996). The organization work force must also be committed to the low-cost strategy.

The intention of firms that utilize cost leadership is to target a large group of customers. Cost leadership refers to an integrated set of measures that are taken to produce goods and services with characteristics that are acceptable to customers at the lowest cost, relative to competitors. Firms usually sell standardized goods or services to the most typical customers of the industry, (Bauer, 2011). Attempts to reduce costs spreads through the whole business process, in products, from manufacturing to the final stage of selling .Any processes that do not contribute towards minimization of cost base are usually outsourced to other organizations with the view of maintaining a low cost base, (Helms, 2012). Low costs enable the firm to offer relatively standardized products or services, which will help the firm gain sustainable competitive advantage, increase profitability and increase its market share (Porter, 1980).

Decision makers in a cost leadership firm, must be compelled to closely scrutinize the cost efficiency of the processes of the firm. Maintaining a low cost base should become the primary determinant of cost leadership. Seth, (2013), states that for low cost leadership to be effective, a firm should have a large market share. New entrants may not benefit from cost leadership since mass production, mass distribution and economies of scale may not make an impact on the new entrants. Cost leadership becomes a defense mechanism against competitors in a highly competitive industry (Parker, 2014). Eventually, cost leadership generates sustainable competitive advantage in a firm therefore high performance.

To succeed at operating at lowest costs while still achieving profitability and high returns, can be achieved in three main ways (Scholes, 2010).The first approach is achieving low direct and indirect operating costs. This can be achieved by offering high volumes of standardized products and limiting customization and standardization of services. Production cost is kept low by fewer and standard components and limiting the number of models produced, to ensure larger production runs, (Allen, 2012). Overheads are kept low by paying low wages, locating premises in low rent areas, and establishing a cost conscious culture in the organization. Costs like research and development and advertising are also minimized.

The second approach is achieving a high asset turn over. This involves production of high volumes of output. This approach aims at spreading fixed costs over a large number of units of the product or service, resulting in a lower unit cost. In this case, the firm aims at taking advantage of economies of scale, and experiencing curve effects, (Baker, 2014). Higher levels of output require and results in high market share, therefore creating a barrier to entry to potential investors who may be unable to achieve the scale necessary to match the firm's low cost and prices.

The third approach is control over the supply chain to ensure low costs. This can be achieved by bulk buying to enjoy quantity discounts, squeezing supplier on price, instituting competitive bidding for contracts and working with vendors to keep investors low using inventory methods such as Just In Time. An example is Wal-Mart which is famous for squeezing its suppliers to low prices for its good, making it the world's largest company, (Buzzell, 2010). Dell computer initially achieved market share by keeping inventories low and only building computers to order. Therefore, firms can offer cost leadership by, Using efficient and low cost distribution channels, utilizing economies of scale through mass production and mobilization of employees, having an easy access to low cost source of capital, and developing cost effective products and services, (Seth, 2013).

It is assumed that cost leadership strategy is only viable for big firms with the ability to enjoy economies of scale and large production volumes. However, small businesses can also use cost leadership if they utilize the advantages of low costs. For example a business in a low rent location can attract price sensitive customers (Malburg, 2010).

David, (2014), states that, another objective of cost leadership is efficiency, the degree to which per unit of output is low. It can be categorized into cost efficiency, and asset parsimony. Cost efficiency measure the degree to which costs per unit are low. Asset parsimony, it is the reduction or minimization of assets used in making a product or service. It is the degree to which assets per unit of output are low. They both capture the firm's cost leadership orientation. This helps the firm improve its performance. Cost leadership also has some disadvantages. Lack of customer loyalty is one of them, as price sensitive customers will always switch the moment a lower price product or service is introduced into the market, (Green, 2013). As cost leadership objective is to reduce costs, this might result to low quality products or services which might ruin the firm's reputation. Also, low prices will result in creating a negative attitude towards the quality of the product in the mindset of customer, (Miller, 2014).

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2.2 Relationship Between Cost Leadership and Performance

The figure below explains the relationship among variables in the situation being examined. It assists in testing the relationship among variables and therefore improving the understanding of the situation.

Independent Variable

Cost Leadership Strategy
- Low direct and indirect operating costs
- Economies of scale
- Easy access to low cost source of capital
- Outsourcing functions and joint ventures

→

Dependent Variable

Performance
- Profitability
- Customer loyalty
- Market share
- Return on Investments

Figure 2.1: Cost Leadership Strategy and Performance of Life Assurance Companies

3. RESEARCH METHODOLOGY

3.1 Research Design

Descriptive research design was used in the study; this is because it seeks to establish factors associated with certain occurrences, outcomes, conditions or types of behavior. It describes the current conditions, terms or relationships concerning a problem, (Maxwell, 2012). Descriptive research design is used when the collected data is analyzed in order to describe the current conditions, terms or relationships concerning a problem.

3.2 The Target Population

The target population of this study was all the life assurance companies in Kenya, which are 26 companies in total. The unit of analysis was comprised of life top managers, middle managers and line managers from the 26 life assurance companies in Kenya. The list of the life assurance companies is attached.

Table: 3.1 Target Population

Category	Population	Percentage
Senior Managers	130	17
Middle Managers	260	33
Line Managers	390	50
Total	780	100

Source: Researcher (2017)

3.3 Sampling Design and Sample Size

This study used systematic random sampling to obtain a sample of 5 life assurance companies out of the 26 companies in Kenya. In systematic random sampling, every k^{th} element in the total list is chosen systematically for inclusion in the sample. In this case, in a total of 26 life assurance companies, every fifth element was selected for the sample (Collis, 2013). Thereafter, all the managers from the selected 5 life assurance companies were studied. Systematic random sampling was the most appropriate for this study because, of the assurance that the population was evenly sampled.

Table 3.2: Sample Size

Category	Sample Size	Percentage
Senior Managers	25	17
Middle Managers	50	33
Line Managers	75	50
Total	150	100

Source: Researcher (2017)

3.4 Data Collection Procedures

Primary data was collected using questionnaires as the main tool for data collection which was dropped and picked later from the respondents. The questionnaires had both open and closed-ended questions. Questionnaire was preferred for this study because it was efficient, cheap and easy to administer (Berger. 2013). Secondary data was collected using a checklist to collect information on profitability and return on investments of the life assurance companies for the last five years.

3.5 Pilot Study

Piloting allows for pre-testing of the research instruments, in this case, questionnaires. Piloting helps the researcher identify questions that are not clear or problems with the questionnaire that might lead to biased answers (Mugenda and Mugenda, 2012). 15 managers were selected from a life insurance company that was not included in the selected sample, and a pre-test with the questionnaires was done.

3.5.1 Data Reliability

Reliability refers to the consistency of measurement instruments (Bonnet, 2010). The instrument in this study is the research questionnaire. This study used Cronbach's alpha to test reliability, a threshold of 0.7 will be used. This was done through Statistical Package for Social Sciences (SPSS) data analysis software.

3.5.2 Data Validity

Validity is the degree to which an instrument measures what it is supposed to measure. Content validity which was employed in this study is the extent to which a measuring instrument provides adequate coverage of the topic under study. The research instrument in this study was the questionnaire; it was checked to ensure that it measured the content it was supposed to measure, and to ensure that the content is meaningful and accurate.

3.6 Data Analysis Procedure and Presentation

Data collected through questionnaires was sorted, edited and cleaned. Coding is whereby researchers assign respondents' answers to pertinent responses categories, in tabulation form, (Creswell, 2013). For quantitative data, descriptive statistics was used. Descriptive statistics included frequencies, measures of central tendencies (mean) and measures of dispersion (standard deviation, correlation and regression Analysis was done through Statistical Package for Social Sciences (SPSS). Data was presented in form of tables, graphs and pie charts.

The study model generated through multiple regression analysis was:

$Y=\beta 0 + \beta_1 X_1 + \mathcal{E}$

Where:

Y= Performance

$\beta 0$= Constant

β_1=Coefficient of variable

X1= Cost Leadership strategy determined by composite of 5 point likert scale

$\mathcal{E}$ = Represents the error term

3.7 Ethical Considerations

Due to sensitivity of some information that was collected, principles of confidentiality and privacy to any information given by the participant were highly adhered to. The rights or free will of the participants was not interfered with including that of ceasing to participation in the research at any time.

4. RESEARCH FINDINGS

4.1 Reliability

Table 4:3 Summary of the Reliability Test Results

Section	No. of items	Cronbach's Alpha	Comments
Cost Leadership	6	0.866	Reliable
Performance	6	0.945	Reliable

Reliability test checks for consistency of measurement instruments. This study used Cronbach's alpha to test reliability, a threshold of 0.7 was used. This study found a reliability of above 0.850 for all variables indicating that the instrument was reliable.

4.2 Regression

The multiple regressions (R) indicates the regression between dependent variable and the independent variables jointly predicted by the model .The multiple coefficient of determination (R^2) determines the changes of variation in dependent variable as explained by dependent variables jointly. The table below shows the values of R and R^2

Table 4.4: Model Summary

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.893[a]	.798	.790	.44059

a. Predictor: (Constant), x1

Source: Author (2017)

In table 4.4 multiple coefficients of variation (R) was 0.893 which implies that the degree of association between performance of life insurance companies and Cost Leadership Strategy is strong and positive. The (R^2) was 79.8% which implies that 79.8 % variations in performance of life assurance companies are explained by Cost Leadership Strategy in the model .while 20.2 % of variations in performance of life insurance companies is explained by random error or other factors.

4.3 ANOVA

Table 4.5: ANOVA

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	76.840	4	19.210	98.962	.000[a]
	Residual	19.412	100	.194		
	Total	96.251	104			

a. Predictor: (Constant) x1

b. Dependent Variable: y

Source: Author (2017

From the ANOVA statistics in the above table, the processed data, which are the population parameters, had a significance level of 0.00 which shows that the data is ideal for making a conclusion on the population's parameter. The F calculated at 5% Level of significance was 98.962 Since F calculated is greater than the F critical (value = 4.76),this shows that the overall model was significant i.e. there is a significant relationship between performance of life insurance companies and Cost Leadership Strategy.

4.4 Coefficients

In determining the cause effect relationship between the dependent variable and the independent variables the regression coefficients were tested at the 5% level of significance using t –test. This is presented in table 4.6 below.

Table 4.6: Coefficients

		Unstandardized Coefficients		Standardized Coefficients		
Model		B	Std. Error	Beta	T	Sig.
1	(Constant)	1.074	.246		4.372	.000
	x1	.156	.177	-.131	.886	.038

a. Dependent Variable: y

4.5 Model Equation

The coefficient of regression table above was used in coming up with the model below:

$Y = 1.074+0.156x1+e$

Where Y is Performance of Life Assurance Companies, x1 is Cost Leadership Strategy. From the model, taking all variables in Cost Leadership Strategy, constant at zero, Performance of Life Assurance Companies in Kenya is 1.074. According to the model, all the variables are significant as their significance value is less than 0.05, Cost Leadership Strategy is positively correlated with Performance of Life Assurance Companies in Kenya.

4.6 Correlation

To determine the degree or strength of linear relationship among the variables, Pearson correlation (r) was used. Linearity increases the predictive power of the model and the validity of the estimated coefficients. The study sought to determine the correlation between the variable in order to determine the strength of the relationship at 1% significance level.
A correlation of r>+0.7 implies that the variable are strongly related negatively or positively

Table 4.7: Correlation

Correlations

‘ +-m

		X1	Y
X1	Pearson Correlation	1	
	Sig. (2-tailed)		
Y	Pearson Correlation	.866**	1
	Sig. (2-tailed)	.000	

Correlations

' +-m

		X1	Y
X1	Pearson Correlation	1	
	Sig. (2-tailed)		
Y	Pearson Correlation	.866**	1
	Sig. (2-tailed)	.000	

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

Source: Author (2017

4.7.1 Correlation between Cost Leadership Strategy and Performance of Life Assurance Companies

Person correlation was used to determine the relationship between cost leadership strategy and performance of life insurance companies The correlation coefficient was 0.866 with p –value (0.000) which was found to be significant at 1% significance level this implies that there exists a strong positive relationship between cost leadership strategy and performance of life insurance companies. An increase in of use cost leadership strategy will lead to an increase in performance of life assurance companies. The results agree with Stephen, (2013) in his study on the effects of strategies adopted by insurance companies to attract business through agents, who found out that performance, is improved if cost leadership is employed in an organization. His results suggested that organizations had employed cost leadership elements to ensure that performance was achieved.

5. SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary of the findings, discussions, conclusions and recommendations emanating from the results of this study.

5.2 Summary of the Major Findings

The study evaluated the effect cost leadership strategy on performance of life assurance companies in Kenya.

The study established that the life assurance companies have employed competitive strategies components with the majority of life assurance companies having highly employed cost leadership strategy.

On association of cost leadership with performance, the study established that life assurance companies in Kenya had highly implemented these cost leadership elements which included, use of low cost distribution channels, advanced technology, access to low sources of capital and training and institutional learning. The study revealed that there was a positive relationship between cost leadership and performance in life assurance companies in Kenya.

5.3 Conclusion

Based on the findings, the study made the following conclusions:

The study established that life assurance companies in Kenya had highly employed cost leadership strategy. Cost leadership had a positive relationship with performance of life assurance companies in Kenya. From the findings, it can be concluded that cost leadership strategy improves the performance of life assurance companies in Kenya, therefore life assurance companies should engage in continuous improvement of the strategy.

5.4 Recommendations

The following are the researcher's recommendation based in the findings of the study that life assurance companies and other stakeholders can use:

Life assurance companies should sustain and continually improve on cost leadership as a competitive strategy by investing more on it. This is because these cost leadership has a significant effect on performance in life assurance companies.

5.5 Suggestion for Further Studies

From the findings the following areas were suggested for further research.

- Strategies adopted by life assurance companies in Kenya to achieve competitive advantage.
- Competitive position strategies adopted by life assurance companies in Kenya.
- Growth strategies adopted by life assurance companies in Kenya
- The influence of organizational learning on performance in life assurance companies in Kenya
- A resource based view approach to performance in life assurance companies in Kenya.

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