DIFFERENTIATION STRATEGIES AND PERFORMANCE OF INSURANCE COMPANIES IN NAIROBI, KENYA

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Abstract: *In Kenya, the present operational set up of the insurance industry is a dynamic one characterized with intense competition due to the presence of numerous insurance organizations. The implication of this is that some firms have experienced poor performance as others succeed. To guarantee survival and sustainability in the market place, firms in this industry must implement competitive strategies, such as, the differentiation strategy. However, differentiation strategy has not been examined in depth in previous studies in relation to performance of insurance firms in Nairobi County, Kenya. Therefore, the objective of the study was to establish the effect of differentiation strategy on performance of insurance companies in Nairobi, Kenya. The study was guided by Porter's Generic strategies. Descriptive survey design was adopted for the study that also targeted 1443 top, middle and lower level managers in 43 insurance companies registered in Nairobi. From these 54 managers were selected for the study using systematic random sampling. Data was collected using pretested copies of a structured questionnaire developed by the researcher were used to collect data. Data was analyzed using both descriptive and inferential statistical methods. The findings revealed that differentiation strategies significantly influenced the performance of insurance firms in the area. Therefore, the study recommends that insurance firms in the area should invest more in continuous training of their personnel to enable them understand the differentiation strategies being pursued by the firm in order to make them more effective in reaching out to the market.*

Keywords: *Differentiation strategy, Generic Strategies, Performance*

1.0 INTRODUCTION

1.1 Background to the Study

In today's turbulent business environment, ability to formulate the future and position the organization or business unit to strategically position with competitive advantage of the potential threats for the survival is of significant impact to the organization (Sauerhoff, 2014). Businesses and even non-business organizations are under increasing competitive pressure to perform if they are to survive and remain relevant in the market (Mahdavian, Mirabi, &Haghshenas, 2014). As such, managers have to be strategic in every aspect of the management function of the organization in the changing business environment characterized by stiff competition, raised stakeholder expectations and the need to maximize utilization of organizational resources by operating more efficiently. However, one of the crucial challenges facing organizations is to build sustainable competitive organizations, and this has been the thrust behind the formation and pursuit of competitive strategies in firms.

Competitive strategies encompass all the actions and tactics that an organization has and is utilizing in attracting customers, survive competition pressure and improve their market position. These strategies are adapted by companies within a particular industry. According to Porter (1998), these strategies which a company implements are expected to influence the performance of the organization. As suggested by Grant (2002), long term strategies need to emanate from an entity's efforts of seeking sustaining competitive edge on foundation of generic strategies, that is, cost leadership, market niche or focus and differentiation strategies. Cost leadership strategies are affected by unique skills of the entity to attain and sustain low cost position within the industry they are operating in. Differentiation strategy is implemented by a company which is endeavoring to produce a product which is unique in the market for different customer segments. Competitive strategies which rely on differentiation are made to be alluring to customers with special sensitivity for a particular attribute in the product. According to Porter (1998), focus strategy is a marketing strategy whereby a firm concentrates its resources on entering or expanding in a small market segment. The strategy is usually employed where the company is aware of its market segment and has a producer service which can competitively satisfy its needs. The focus this paper will be on differentiation strategies.

1.1.1 Differentiation Strategy

Differentiation strategy is an approach under which a company aims to develop and market unique services and products for different customer segments. Differentiation strategy is a marketing practice used by companies in establishment of strong identity in a given market. It can also be defined as a positioning a product or service in a manner that enable differentiating it from the competition and establishment of an image that stands out from the rest (Davison, 2011). It is one of three generic marketing strategies that can be adopted by any insurance firm. Usually employed where an insurance company has clear competitive advantages, and can sustain an expensive advertising campaign. Through the use of this strategy, insurance companies introduce a variety of similar primary services and products under the same name into specified services as well as product categories and therefore cover the different services and product available under the category.

To maintain this strategy, the Insurance company should have: strong research and development skills, strong services and products engineering skills, strong creativity skills, good cooperation with distribution channels, strong marketing skills, and incentives based largely on subjective measures, be able to communicate the importance of the differentiating services and products characteristics, stress continuous improvement and innovation and attract highly skilled, creative personnel. Research within service sector concludes that services and product differentiation is a common way of differentiating the Insurance firm's offerings from those of its competitors (Prescott, 2008).

1.1.2 Firm Performance

Performance is dynamic, requiring judgment and interpretation. Performance may be illustrated by using a causal model that describes how current actions may affect future results. Performance may be understood differently depending on the person involved in the assessment of the organizational performance for example it can be understood differently from a person within the organization compared to one from outside. As firms actively seek to position themselves competitively in the market, and thus achieve performance the subject of strategy and the management roles in strategy development and execution become very important.

Firm performance has been a subject of intense research for many years. Although the concept of organizational performance is very common in the academic literature, its definition is difficult because of its many meanings. Organizational performance has been defined variously from the early 50' to date as the extent to which organizations, viewed as a social system fulfilled their objectives, as an organization's ability to exploit its environment for accessing and using the limited resources in the 60's. As success in accomplishing its goals (effectiveness) using a minimum of resources (efficiency). In The 80's and 90's and today Performance is a set of financial and nonfinancial indicators which offer information on the degree of achievement of objectives and results (Lebans&Euske 2006).Performance is therefore presented as a multidimensional concept (Venkatraman&Ramanujam, 1986). Can be both financial and non-financial (subjective measurements) such as, for example, shareholder satisfaction, employee satisfaction, customer satisfaction (Ong &Teh, 2009).

For a firm to improve its performance, managers design and implement a number of strategies. Many managers in the industry understand their businesses and the strategies required for their success but they still struggle to translate these theories into action plans for successful implementation of strategies.

1.1.2 Insurance Firms in Kenya

Kenya's insurance industry has become competitive because of the drop in demand of non-mandatory insurance services in addition to pessimism from the consumers. According to AKI (2015), the degree of penetration is around 3.03 percent which is extremely low in comparison with 1st world countries, however, in comparison to emerging markets average of 2.7% the industry in the country is considered vibrant and has great potential for growth (AKI, 2016).The industry's annual performance exceeded the overall economic growth of 4.4% recorded in 2015. In 2016, the industry registered improved performance despite the decline in the country's economic growth. The industry recorded gross written premium of Kshs 91.60 billion compared to Kshs 79.06 billion in 2015, representing a growth of 15.9%. The gross written premium for non-life insurance was Ksh 60.67 billion (2015: Ksh 52.35 billion) while that for life insurance was Ksh 30.93 billion (2015: Kshs 26.71 billion). Non-Life insurance premium grew by 15.9% while life insurance premium grew by 15.8% (IRA, 2016).

Nevertheless, the insurance industry is still facing many challenges. The first challenge is to come up with a solution for companies whose viability is threatened by their inability to meet policyholders' claims. The second major challenge is how to generate growth for an industry that has significant potential for growing as a percentage of Gross Domestic Product (GDP). To overcome these challenges individual companies must generate and implement strategies geared towards improving organization's performance in a competitive environment. However, the future of insurance in Kenya is bright given the huge untapped market, increase in the use of Information and Communication Technology (ICT), utilization of alternative distribution channels such as banks and Savings and Credit Co-operatives (SACCOs), research and new product development. Further, the government recognizes the critical role played by insurance as a sector in the economy. It has documented the sector as a major player in the financial sector in the achievement of Vision 2030. Therefore, the survival and prosperity of insurance firms in the future will depend largely on how they position themselves in the market competitively and more so using well known strategies such as the differentiation strategy.

1.2 Problem Statement

In Kenya, the present operational set up of the insurance industry is a dynamic one characterized with intense competition due to the presence of numerous insurance organizations. By 2011, the average growth rate of General Insurance Business was estimated at 15.9%. About 22% of the companies had negative growth, 35% were growing 16% and 32% had 16—50% growth while 11% recorded over 50% growth (AKI, 2015). The implication of this is that some firms have experienced poor performance as others succeed. One factor that has been identified as explaining the difference is strategy implementation. To guarantee survival and sustainability in the market place, firms in this industry must implement competitive strategies. Several research studies have been carried out on competitive strategies in Kenya under varied settings. In a study on competitive strategies adopted by country's financial institutions, Gathoga (2011) established that various tactics are adopted by these entities to maintain competitiveness. In a study of strategies adopted by Real estate firms, Karanja (2002) established Porters generic model strategies are adopted. There is however limited research in this field and specifically relating to insurance industry in Kenya. Further, none has examined the differentiation strategies being pursued by firms in the insurance industry. The present research is meant to fill this gap by establishing the effect of differentiation strategy on performance of insurance companies in Nairobi, Kenya.

1.3 Objective of the Study

The objective of the study was to determine the effect of differentiation strategy on performance of insurance companies in Nairobi.

1.4 Research Questions

The study sought to answer the following question: -

How does differentiation strategy affect performance of insurance companies in Nairobi?

2.0 LITERATURE REVIEW

2.1 Differentiation Strategies and Insurance firms

The basis for competitive advantage is provision of services and products whose attributes differ significantly from rivals' services and products. A differentiation strategy calls for the development of services and/or products that offer unique attributes that are valued by customers and that customers perceive to be better than or different from the services and products of the competition. Successful differentiation is based on a study of buyers from different places needs and behavior in order to learn what they consider important and valuable. The desired features are then incorporated into the services and products to encourage buyer preference for the services and products. Efforts to differentiate often result in higher costs.

Oakland (1999) noted that there are at least two different types of differentiation strategy: those based on services and products innovation and those based on intensive marketing and image management. The key success factors which contribute to the profitability of a differentiator include creative flair, strong basic research services and products engineering (Malburg; 2000; Porter, 1998). Profitable differentiation is achieved by either keeping the cost of differentiation below the price premium that the differentiating features command, or by offsetting the lower profit margins through more sales volumes (Grant, 2002).

A service and a product can be differentiated in various ways. Unusual features, responsive customer service, rapid services and products innovations and technological leadership, perceived prestige and status, different tastes, and engineering design and performance are examples of approaches to differentiation (Porter, 1998). Rather than cost reduction, a firm using the differentiation strategy needs to concentrate on investing in and developing such things that are distinguishable and customers will perceive. Overall, the essential success factor of differentiation in terms of strategy implementation is to develop and maintain innovativeness, creativeness, and organizational learning within an organization.

Hyatt (2011) insists that anything that an organization can do to create buyer value represents a potential basis for differentiation. Once it finds a good source of buyer value, it must build the value, creating attributes into its services and products at an acceptable cost. These attributes may raise the services and products' performance or make it more economical to use. Differentiation possibilities can grow out of possibilities performed anywhere in the activity cost chain. Porter (1998) suggested that an organization may obtain a competitive advantage by creating a higher value for its customers than the cost of creating it, either by adopting a differentiation strategy or an efficiency strategy. Organizations pursuing a differentiation strategy attempt to differentiate themselves from their rivals using a variety of sales, marketing and other related services or product and technology innovations. An organization adopting a differentiation strategy commands above-market prices made possible by the customers perception of the services and products being special in some way.

Differentiation relates to the degree to which a services and products and its enhancements are perceived as unique. In the insurance industry, the value added by the uniqueness of the services and products may allow the insurance company to charge a premium price for it. The insurance company hopes that the higher price will more than cover the extra costs incurred in offering the unique services and products. Because of the services and products' unique attributes, if suppliers increase their prices the insurance company may be able to pass along the costs to its customers who cannot find substitute services and products easily (Porter, 1998). The insurance company that succeed in a differentiation strategy often have access to leading scientific research, highly skilled and creative services and products development team, strong sales team with the ability to successfully communicate the perceived strengths of the services and products and corporate reputation for quality and innovation (Prescott, 1998).

With the differentiation strategy, unique attributes or perceptions of uniqueness and characteristics of an insurance company services and products other than cost provide value to customers. The insurance firm pursuing differentiation seeks to be unique in its industry along some dimension that is valued by customers, which means investing in services and products, research and development (R & D) and marketing (Porter, 1980). It is the ability to sell its differentiated services and products at a price that exceeds what was spent to create it that allows the insurance company to outperform its rivals and earn above-average returns (Dess& Davis, 1984).

2.2 Porter's Generic Strategies

Porters (1998) generic strategies entails low cost, differentiation as well as combination of two or more of these strategies. According to Porter (1985) firms' major concern is the extent of completion in the industries they are operating in. Porter's hypothesis that low cost and differentiation strategies are at distinct end of continuum and that they are in no way related to each other has led to theoretical debate and empirical studies. The debate partly emanates from lack of conceptual building blocks that supports Porter's value system. Consequently, researchers have come with hypothesis arguing against porter's Point of view, and suggesting that low cost and differentiation may in fact be independent dimensions that need to be strongly pursued simultaneously (Fournier, 2008). Empirical research utilizing the MIS database by Miller and Dess (2010) opine that the generic strategy framework may be fostered through perceiving cost and differentiation as two dimensions of strategic positioning as opposed to viewing them as two discrete strategies. The idea that pursuing of numerous sources of competitive advantage is both practicable and appropriate has been supported by more researchers (White, 2008).

Through Porters value chain approach, attractiveness of the industry can be determined. Using their knowledge on the intensity and impact of competitive forces, companies in the insurance sector are then in a position to develop options for influencing in a way that enhances their competitive standing. To be able to survive, the insurance companies need to adapt tactics that are applicable to the dynamic market place. The winning tactic chosen can alter the impact of competitive forces on the organization. The primary aim here is decreasing the power of competitive forces. Despite the fact that many companies following cost and differentiation strategy at the same time may be trapped in the middle, evidence exists of some companies that have attained economic performance through adoption of the two strategies (Bresnahan& Reiss, 2010). Porter's generic competitive strategies provided suitable grounds to test the assumptions of differentiation strategies employed by the insurance firms and establish whether the firms were purely pursuing differentiation or a hybrid strategy incorporating the best features of differentiation and cost leadership.

3.0 METHODOLOGY

3.1 Research Design

Descriptive survey design was adopted for the study. This research design fitted the study since it is an efficient method for systematically collecting data from a broad spectrum of individuals making it possible to collect a large amount of data on the study problem with minimum effort. It also enables generalizations to be made on the outcome of the study (Kombo & Tromp, 2009).Borg and Gall (1996) recommended descriptive survey design for its ability to produce statistical information about aspects of insurance that interest policy makers and researchers.

3.2 Target Population

The population of interest for this study comprised of all the 43 insurance companies registered in Nairobi as of December 2017. The accessible population was the management of the insurance firms because they are the ones involved in strategy formulation and implementation. Data from the human resource management of the various firms puts the total number of managers, that is, lower level, middle level and top level at 1443 persons.

3.3 Sample Size and Procedure

Since the population of interest to the study is sufficiently large to warrant probability sampling, the actual sample size was obtained using the method recommended by Nassiuma (2000);

$$n = \frac{Nc^2}{c^2 + (N-1)e^2}$$

Where n = sample size, N = population size, c = coefficient of variation (≤ 30%), and e = error margin (≤ 5%). In this study c was taken as 30%, *e* to be 4% and N = 1443, therefore, fitting this into the formula:

$$n = \frac{1443 * (0.3)^2}{(0.3)^2 + (1443-1) * (0.04)^2} = 54.18 \approx 54$$

Therefore, the study 54 managers were selected for the study. Systematic random sampling was used to select the respondents using predetermined sampling intervals to ensure every firm was involved in the study. This method ensures that large populations can be analyzed with every member of the population having an equal chance of being included, therefore, minimizing bias (Kombo & Tromp, 2006).

3.4 Data Collection

Copies of a structured questionnaire developed by the researcher were used to collect data. The questionnaires were preferred in this study because respondents of the study were literate and quite able to answer questions asked adequately. According to Mugenda and Mugenda (2003), questionnaires are commonly used to obtain important information about a population under study. The questionnaire was carefully designed and tested with among a pilot group of seven respondents from selected insurance firms. This was done in order to enhance its validity and reliability for accuracy of data to be collected for the study.

The validity of the instrument was determined through content validity. This was done by subjecting the questionnaire to scrutiny and review by the researcher's supervisors at the University to ensure that all the items used in the questionnaires are consistent and valid. Some items were, however, rephrased and modified to avoid ambiguity before being used for data collection.

In this study reliability test was done on all the variables of the questionnaire. Cronbach's Alpha coefficient was used as a test for the reliability of the instrument. Cronbach alpha values of 0.7 and above are recommended and was considered adequate (Cronbach & Azuma, 1962). The study's instrument yielded Cronbach's Alpha values above 0.7 for all variables as shown in Table 1.

Table 3.2 Cronbach's Alpha value of variables

Variables	Cronbach's Alpha	Number of Items
Differentiation	0.852	7
Performance	0.719	3

3.5 Data Analysis

Data was analyzed using both descriptive and inferential statistical methods. Descriptive statistical analysis will be done using, frequencies and percentages to describe the basic characteristics of the data. Inferential data analysis will be done using the Pearson's Product-Moment Correlation Coefficient. Correlation analyses will used to measure the relationship between variables. The importance of this is that the results of the analysis can be generalized to the larger population.

4.0 RESULTS AND DISCUSSIONS OF FINDINGS

A total Number of 54 instruments were administered to staff in the 9 selected insurance firms in Nairobi, Kenya. All the questionnaires were dully filled and returned hence the response rate was 100%.

4.1 Differentiation Strategy in the Insurance Firms

The study sought to explore the extent to which differentiation strategies used in the insurance firm based on various aspects. The findings are presented in Table 2.

Table 2: Differentiation strategy and Performance of Insurance firms

Statement	Very great extent	Great extent	Moderate extent	Little extent	Not at all
Differentiation based on product/service	52(96.3%)	2(3.7%)	0(0.0%)	0(0.0%)	0(0.0%)
Differentiation based on price	37(68.5%)	7(13.0%)	10(18.5%)	0(0.0%)	0(0.0%)
Differentiation based on place	10(18.5%)	24(44.4%)	20(37.0%)	0(0.0%)	0(0.0%)
Differentiation based on promotion/ advertising campaign	18(33.3%)	16(29.6%)	12(22.2%)	8(14.8%)	0(0.0%)
Differentiation based on personnel	35(64.8%)	8(14.8%)	7(13.0%)	4(7.4%)	0(0.0%)
Differentiation based on image	43(79.6%)	5(9.3%)	1(1.9%)	5(9.3%)	0(0.0%)
Differentiation based on technological Leadership	42(77.8%)	4(7.4%)	8(14.8%)	0(0.0%)	0(0.0%)

The findings in Table 2, it was clear that differentiation based on product/service was used to a very great extent in most firms as expressed by majority (96.3%) of the respondents. Most firms also practiced differentiation based on price (68.5%). Majority (44.4%) of the respondents had the opinion that their firms practiced differentiation based on place. Differentiation based on promotion or advertising campaign was also practiced in the insurance firms as indicated by majority (33.3%) of the respondents. The findings also indicate that most firms carried out differentiation based on personnel (64.8%) and image (79.6%) respectively. In addition, differentiation based on technological leadership was also practiced in the firms (77.8%). In general, it is evident that several aspects of differentiation strategy were being pursued by the insurance firms although in varying degrees with more emphasis being placed on differentiation based on product/service than the other aspects. Differentiation based on place and on promotion/ advertising campaign were not being given strong considerations, however.

4.2 Performance of Insurance Firms

The study also sought to establish the performance of insurance firms in Nairobi County. The findings are presented in Table 3.

Table 3: Trend of Various Aspects in the organization for the Last Five Years

Statement	Greatly Improved	Improved	Constant	Decreasing	Greatly Decreased
Revenue has increased in the last five years	34(63.0%)	20(37.0%)	0(0.0%)	0(0.0%)	0(0.0%)
Quality of the service	32(59.3%)	16(29.6%)	6(11.1%)	0(0.0%)	0(0.0%)
Increasing no. of new customers in the last five years	27(50.0%)	6(11.1%)	21(38.9%)	0(0.0%)	0(0.0%)

From the findings, it was evident that revenue had greatly improved for the last five years as expressed by 63.0% of the respondents. Majority (59.3%) of the respondents were of the view that quality of service had greatly improved in the last five years and the firms had been able to attract new customers in increasing numbers in the last five years (50.0%). These findings imply that generally the performance of the insurance firms in the area was on the increase as indicated by the measures. The increase in revenue arose primarily to the increased product uptake which is a good sign of the impact of the differentiation strategy. The observation that new customers were increasing in the firms could also explain the effect differentiation strategy was having on the performance of the firms.

4.4 Hypothesis Testing

Correlation analyses will used to measure the relationship between differentiation strategy and the performance of the insurance firms in the area. Table 4 gives the correlation analysis results.

Table 4: Correlation results between differentiation and performance

Variable		Correlation	Sign
Independent Variable			
	Performance of Insurance Firms		
Dependent Variable			
	Differentiation	0.427	0.001
	N= 54		

From the results in the above Table 4, it was established that there was a significant moderate positive relationship between differentiation strategy and performance of the insurance firms as indicated by the correlation coefficient of 0.427, $p \leq 0.05$. The implication of the above results is that differentiation strategy only moderately influenced the performance of the insurance firms. The results of this study concurs to those obtained by Gathoga (2011) in a study on competitive strategies adopted by commercial banks in Kenya, which established that there was a positive association between utilization of competitive strategies and their performance.

5.0 DISCUSSION OF FINDINGS

From the foregoing findings, it is evident that the insurance firms in the area were employing several aspects of differentiation strategy. The findings also revealed that the firms used differentiation strategies that were service/product oriented and marketing and image leaning. These findings agree with Oakland (1999) who observed that firms employed at least two different types of differentiation strategy: those based on services and products innovation and those based on intensive marketing and image management. These findings also provide empirical evidence in support of the differentiation strategies argued by Porter (1998) in his generic strategies that a service and a product can be differentiated in various ways. These include unusual features, responsive customer service, rapid services and products innovations and technological leadership, perceived prestige and status, different tastes, and engineering design and performance are examples of approaches to differentiation. However, they tended to stress some more than others, such as, differentiation based on product/service than differentiation based on place and on promotion/ advertising campaign.

These findings on performance also suggested that the increasing revenues in the firms could likely be a function of the differentiation strategy as opposed to the cost leadership strategy. The latter was not evidenced in the findings and, hence, it is possible that the firms were not pursuing an admixture of both strategies as had been implied by previous researchers examining the generic strategies (White, 2008; Bresnahan& Reiss, 2010). Hyatt (2011) had argued that an organization adopting a differentiation strategy commands above-market prices made possible by the customer's perception of the services and products being special in some way. Further, the observation that new customers were increasing in the firms could also explain the effect differentiation strategy was having on the performance of the firms with the argument by Hyatt (2011) that anything that values addition through the differentiation strategy is an important tool for creating new customers.

5.2 Conclusion

The study established that several aspects of differentiation strategy were being pursued by the insurance firms although in varying levels of emphasis with differentiation based on product/service being stressed more than the other aspects such as differentiation based on place and on promotion/ advertising campaign. The study,therefore, concludes that the firms were keen on adding value to their products to increase their visibility and customer experience more than on creating publicity for them. The findings also revealed that generally the performance of the insurance firms in the area was good leading to the conclusion that using the differentiation strategy had a positive impact on the firms. The theoretical implications of the study are that the firms were capable of pursuing the differentiation strategy in two ways: those based on services and products innovation and those based on intensive marketing and image management. However, no basis was found to support the view that the (insurance) firms were pursuing cost leadership and differentiation strategies at the same time.

5.3 Recommendations

Based on the findings, the study recommends that managers need to ensure that the message of differentiation reaches the clients promptly, as the customer's perceptions of the institution are significant.

The study further recommends that in order for insurance firm to enhance their performance then they should invest more in continuous training of their personnel to enable them understand the differentiation strategies being pursued by the firm in order to make them more effective in reaching out to the market.

5.4 Suggestions for Further Research

The study recommends the following areas for future research; the effect of hybrid generic competitive strategies on performance of insurance firms and also the influences of diversification strategies on competitiveness of insurance firms in Kenya.

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Sources of Funding

This entire research work from conceptualization to publication in this journal has been funded by the author **Stephen Mori Scaver Msinga.** No extra funding has been sourced from elsewhere.