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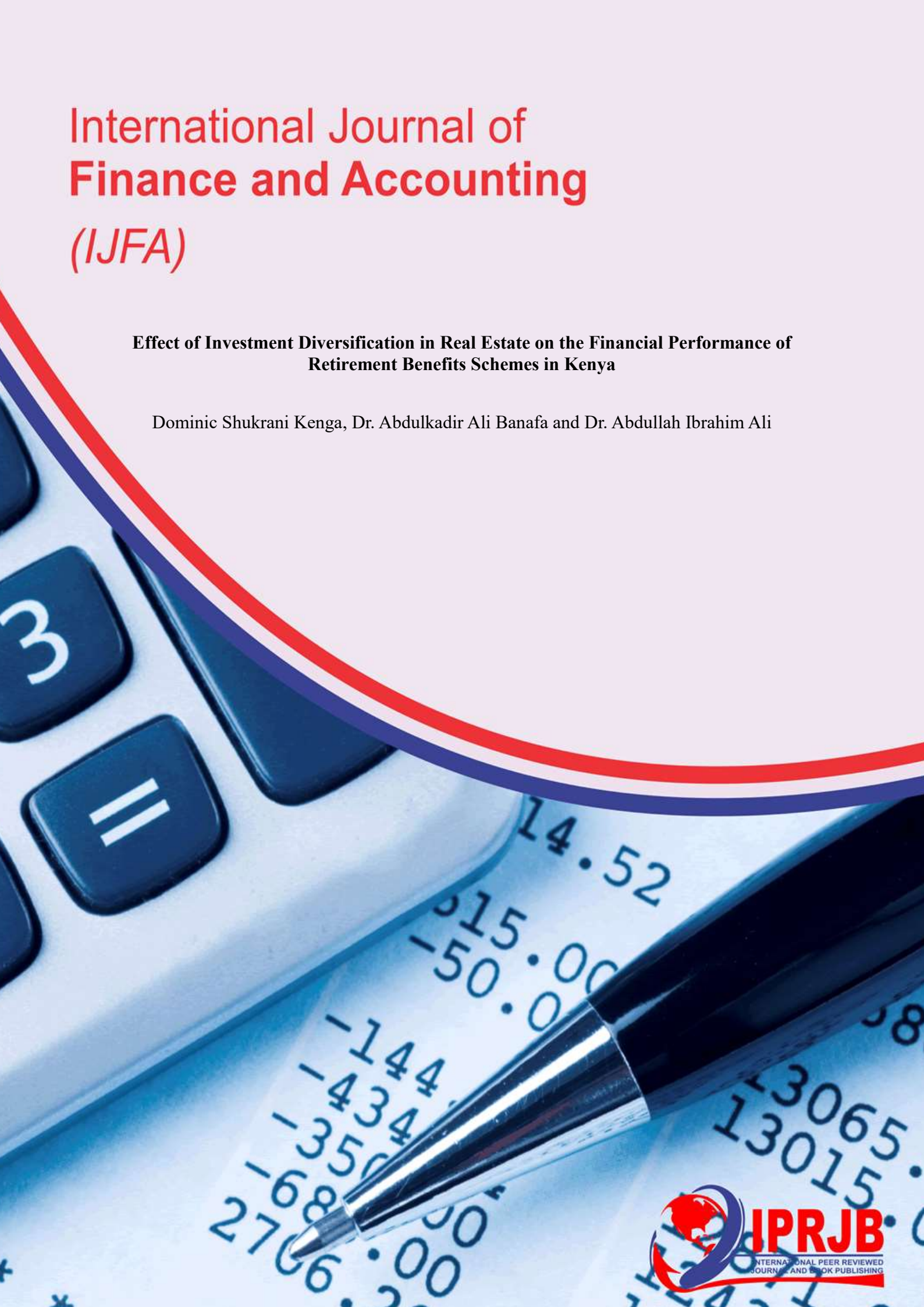

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Effect of Investment Diversification in Real Estate on the Financial Performance of Retirement Benefits Schemes in Kenya

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Abstract

Purpose: Prudence investment calls for investment diversification so as to subvert the tendon of subpar performances. The study investigated the effect of investment diversification in real estate on the financial performance of the retirement benefits schemes in Kenya. The study further investigated the moderating effect of the foreign exchange rate on the relationship between the independent and the dependent variable.

Methodology: The study embraced a descriptive research design and the study population constituted of 87 retirement benefits schemes. The stratified random sampling technique used resulted into having 72 units of analysis. Primary and secondary quantitative data were employed in this study. The primary data was collected using questionnaires, whereas the secondary data was collected via data observation schedules. Data analysis was through the regression model enshrined in the statistical package for social sciences version 20.

Findings: The hypothesis testing led to the rejection of $H_{01,}$ and $H_{02.}$ The rejection H_{01} confirmed that investment diversification in real estate has a significant positive effect on the financial performance of the retirement benefits schemes in Kenya. The rejection of H_{02} confirmed that foreign exchange rate has a significant positive moderating effect on the relationship between investment diversification in real estate and the financial performance of the retirement benefits schemes in Kenya.

Unique Contribution to Theory, Practice and Policy: The study supported the Modern Portfolio Theory (MPT) which advocates for investors to build optimal investment portfolios out of the risky assets at their disposal through diversification so as to arrive at an optimal investment portfolio. The concept of investment diversification is essential since it presents investors with an opportunity of not losing everything, since when one asset within their portfolio fails, the loss may be borne by the other assets within the same investment portfolio which will have posted positive returns on investment. The study recommends that the retirement benefits authority should devise policies which support investment diversification in the retirement benefits schemes.

Keywords: *Real Estate, Investments Diversification, Portfolio, Financial Performance, Retirement Benefits Schemes*

INTRODUCTION

Investment diversification refers to a scenario where a company undertakes various types of investments with different inherent risks as opposed to committing all its finances in one investment (Kioko & Ochieng, 2020). This concept is in congruent with the old adage of not putting all your eggs in one basket (Aregu & Tassew, 2018). As a result of investment diversification, people can invest in various financial securities such as equities, bonds as well as government securities through the commercial banks, pension schemes as well as the investment banks (Kiboi & Bosire, 2022). It is anticipated that as the financial intermediaries diversify their investment portfolios, their financial performance will upsurge (Aregu & Tassew, 2018). This current research sought to undertake an investigation regarding the investment diversification in real estate. Globally, companies have been embracing diversification in real estate and this has positively contributed to their financial performances (Choi, Fedenia, Skiba, & Sokolyk, 2017). In the region of Africa as well as in the local perspective in Kenya, those companies which practiced investment diversification also reported positive performance results (Kioko & Ochieng, 2020)

Statement of the Problem

The performance of the retirement benefits schemes in Kenya has not been optimal over the years as portrayed in its contribution to the country's GDP which stood at 13.3% in 2020 as well as increased complaints from investors (Muli & Ambrose, 2022). The subpar performance can be attributed to lack of investment diversification, since studies around the globe shows that embracing investment portfolio diversification has a tendency of subverting the poor performance of entities into superior performances (Kioko & Ochieng, 2020).

In response to the problem of poor financial performance in the retirement benefit schemes in Kenya, as well as the methodological, contextual and conceptual research gaps emanating from previous research studies, this present study sought to conduct an investigation in an attempt to unravel the effect of investment diversification in real estate on the financial performance of retirement benefits schemes in Kenya.

Objectives of the Study

i. To determine the effect of investment diversification in real estate on the financial performance of retirement benefits schemes in Kenya.
ii. To investigate the moderating effect of foreign exchange rate on the relationship between investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya.

Hypothesis

H_{01}: Investment diversification in real estate has no significant effect on the financial performance of retirement benefits schemes in Kenya.

H_{02}: Foreign Exchange rate has no significant moderating effect on the relationship between investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya

LITERATURE REVIEW

The Modern Portfolio Theory

The Modern Portfolio Theory (MPT) was initially propagated through the portfolio selection seminal works of Markowitz in his 1952 paper (Markowitz, 1952). The central focus of the

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MPT theory is on how risk averse investors could construct portfolios which maximizes expected returns within certain acceptable market-wide risks (Mehmood, Hunjra, & Chani, 2019). The theory advocates for investors to build optimal investment portfolios out of the risky assets at their disposal through diversification such as mixing risky assets with risk free assets in an attempt to arrive at an optimal investment portfolio (Hutagaol & Dharmastuti, 2022). This concept of investment diversification propagated by the theorists is in the premise of the old adage of not carrying all eggs in one hamper (Ringera & Muturi, 2019). Diversification of investment portfolios presents investors with an opportunity of not losing everything, since when one asset within their portfolio fails, the loss may be borne by the other assets within the same investment portfolio which will have posted positive returns on investment (Wahyudi, Hasanudin, & Pangestuti, 2020)

The MPT theory was among the preliminary abstemious hypothetical exertion in quantifying the association amid risk and recompense (Aregu & Tassew, 2018). The concept describes risk through the employment of statistical techniques such as variance and standard deviation as the improbability of returns (Ehiedu & Chika, 2022). Therefore, investors ought to take in account the intrinsic risks enshrined in any expected recompense when constructing their investment portfolios (Hutagaol & Dharmastuti, 2022). With this in mind, it is therefore possible for investors to construct an "efficient frontier" which could contribute optimal returns on investment within a given level of risk (Makau & Jagongo, 2018). The MPT theory has been the blue print for researchers around the globe on investment and financial performance such as Mehmood, Hunjra and Chani (2019) in South Asia, Ehiedu and Chika (2022) in Nigeria, as well as Ringera and Muturi (2019) in Kenya.

Conceptual Framework

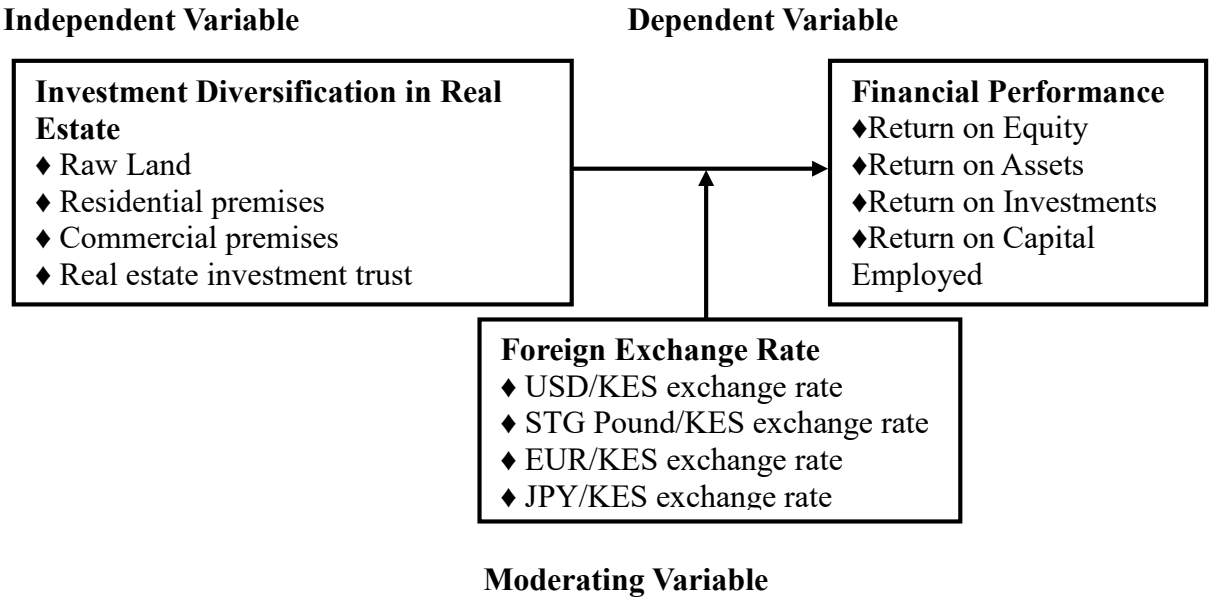

Figure 1: Conceptual Framework

Empirical Review

Makau and Jagongo (2018) conducted a research study on investment diversification and financial performance of investment entities at the NSE. The authors employed the exploratory research design whereas data analaysis was through the regression model. The research study

was supported by the Mrkowitz MPT as well as the capital markets theories. The scholars concluded that investment portfolio diversification in real estate has a significant positive effect on the financial performance of investment companies listed at the NSE as measered by ROA and ROE. In their study on investment portfolio diversification and financial performance, Kioko and Ochieng (2020) resolved that investment in real estatet has a significant positive effcet on financial performance. The research investigated the investments entities operating at the NSE. The study adopted the descriptive research design and data analysis was via the multiple regression statistical model.

In their study on investment porfolio diversification and financial performance, Muthui and Wephukulu (2019) cocncluded that investment diversification in real estate has a significant positive effect on fininacial performance. The study was supported by the MPT as well as the the arbitrage theories. The researchers espaoused the descriptive research approach whereas the seondary data was analyzed through the regression statistics in SPSS. In a similar endeavor, Kiboi and Bosire (2022) concluded that investment in equities has a significant positive effect on financial performance. The researchers used the simple linear regression technique in their study. In another study on the effect of investment diversification and financial performance, Rop, Kibet and Bokongo (2016) resolved that investment diversification in real estate affect financial performance. The researchers used the exploratory research design and their secondary data was analyzed through the regression model.

Research Gap

The reviewed empirical literature brought about the research gap which this study endeavored to address. For instance, the study by Makau and Jagongo (2018) was done in at the Nairobi Securities Exchange and not in the retirement benefits schemes. The study by Kioko and Ochieng (2020) used the multiple linear regression model as opposed to the simple linear regressionnmodel used in this study. Again none of the researchers conceptualised their study variables in the same way as in this present study. In response to the contextual, methodological and conceptual research gaps, this study conducted an investigation in an attempt to unravle the effect of investment diversification in real estate on the financial performance of retirement benefites schemes inKenya.

MATERIAL AND METHODS

The descriptive research design was employed in this study, whereas the population for the study comprised of the 87 retirement benefits schemes in Kenya. The Yamane Taro 1967 formular employed in determining the sample size resulted into having a total sample size of 72. The stratified random sampling technique was used in selecting the 72 units of analysis out of the population. Data for the study was collected via questionnaires and data observation schedules. The collected was analyzed through the Statistical Package for Social Sciences version 20. Descriptive statistics, correlation statistics as well as the regression statistics were generated in this study. Diagnostic tests were conducted on the data before running the simple linear regression model. The regression coefficients generated were used in testing the hypothesis at 0.05 level of significance and decision made on whether to reject or fail to reject the null hypothesis. The regression model guiding this study was formulated in the following manner.

$$Y = \beta_0 + \beta_1 X_1 + \varepsilon \quad \text{Equation 1}$$

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Where:

Y: Represented the Financial performance

X_1: Represented investment diversification in real estate

The moderated regression model was espoused in determining the moderation effect of the foreign exchange rate on the relationship between investment diversification in equities and the financial performance of the retirement benefits schemes. The moderated regression model was specifically employed in testing for H_{02}. The moderated regression model tests whether the prediction of a dependent variable (Y), from an independent variable (X) varies across levels of a moderating variable (Z). The moderated regression model comprised of two stages, the first stage involved estimating the main effect of the predictor variable (X) and the hypothesized moderator (Z) as shown in equation 2.

$$\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_Z Z + \varepsilon} \quad \textbf{.....Equation 2}$$

Where:

Z: Represented the moderating variable (Foreign exchange rate)

β_Z: Represented the beta coefficient of the moderating variable

The second stage encompassed adding the interaction of the moderating variable so as to obtain equation 3.

$$\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_{1Z} X_1 * Z + \varepsilon} \quad \textbf{.....Equation 3}$$

Where:

β_{1Z}: Represented the beta coefficients of the product term (X*Z)

DISCUSSION AND FINDINGS

Test for Normality

For the successful running of the linear regression model, the data ought to be distributed normally (Creswell & Creswell, 2022). Normality of the data is confirmed when the normal (Probability to Probability) (P-P) plot tends to follow a liner pattern (Kothari & Garg, 2019). Figure 2 shows that the data points in the P-P plot follow a linear distribution pattern, thus confirming that the data set was normally distributed.

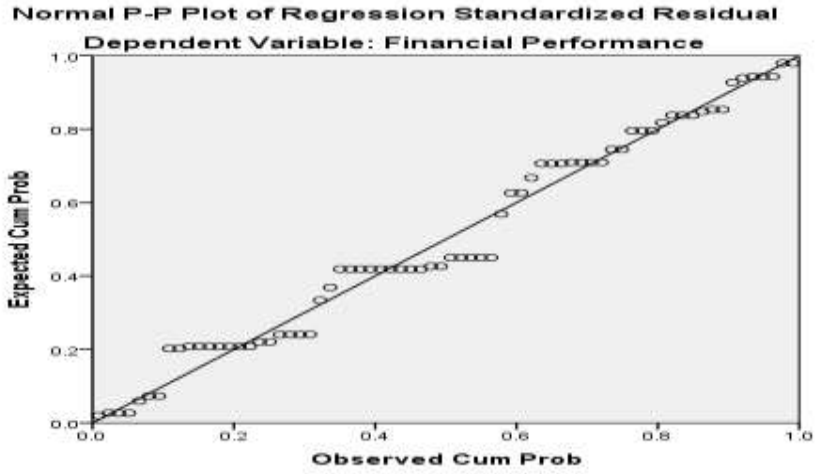

Figure 2: Normal P-P Plot

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Test for Linearity

The scatter plots enshrined in SPSS were used in testing for linearity (Field, 2017). Researchers confirm the presence of linear relationship between the independent and the dependent variables when the scatter plot portray an oval shape distribution (Holmes, 2019). The oval shape distribution pattern of the scatter plot presented in figure 3 confirmed the presence of linearity, thus paving way for the successful application of the linear regression model.

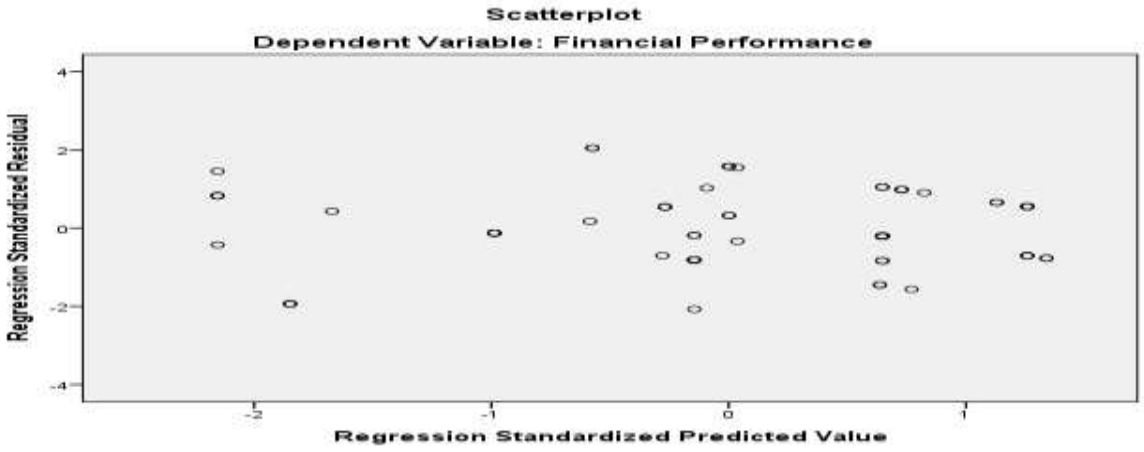

Figure 3: Scatter Plot

Descriptive Statistics

The descriptive statistics for the investment diversification in bonds were generated using SPSS and the results tabulated in Table 1.

Table 1: Descriptive Statistics

	N Statistic	Minimum Statistic	Maximum Statistic	Mean Statistic	Std. Deviation Statistic
Investment Diversification in real estate	70	3.50	4.75	4.2536	.57340
Moderated Investment Diversification in real estate	70	3.00	5.00	4.5000	.73721

Table 1 depicted that the overall mean for the investment diversification in real estate variable was 4.2536, thus portraying the general agreement by the respondents that the retirement benefits schemes incorporated real estate in their investment portfolio. The standard deviation statistics value of 0.57340 which was less than the mean value indicated that the data for the investment diversification in bonds was well distributed around the central tendency. Again, the mean statistics of 4.5000 and the standard deviation of 0.73721 for the moderated investment diversification in real estate showcased that data was well dispersed around the mean.

Pearson's Correlation Analysis

The Pearson's corelation coeficients test the strenght of the relationship between the dependent and the independent variables under inquiry (Kothari & Garg, 2019). The dependent varaible for this study was financial opoerformance, whereas the indpendent varaibale was investment diversification in rweal estate. The Pearson's correlation analysis statistics were generated and tabulated in Table 2.

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Table 2: Pearson's Correlations Coefficients

		Financial Performance	Investment Diversification in Real Estate	Moderated Investment Diversification in Real Estate
Financial Performance	Pearson Correlation	1		
	Sig. (2-tailed)			
	N	70		
Investment Diversification in Real Estate	Pearson Correlation	.371**	1	
	Sig. (2-tailed)	.002		
	N	70	70	
Moderated Investment Diversification in Real Estate	Pearson Correlation	.402**	-.135	1
	Sig. (2-tailed)	.001	.266	
	N	70	70	70

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

The pearson's correaltion analysis outcomes presented in Table 2 indicated a strong positive ralationship of 0.371 between investment diversification in real estate and financial performance, which was significant at 0.05 level (2-tailed). The outcomes indicated that for every unit increase in investment diversification in real estate, financial performance increases by 0.371 units.The corelation coeficient for the moderated relationship bewteen investment diversification in real estate and financial performance was a strong positive 0.402.

Regression Analysis

This section comprised of the Table 3 for the model summary, Table 4 for the ANOVA table and Table 5 for the regression coefficients of the direct relationship model. Table 6 was used to represent the regression coefficients for the moderated relationship model.

Table 3: The Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.644[a]	.414	.378	.39811

a. Predictors: (Constant), Investment Diversification in real estate, Moderated Investment Diversification in real estate
b. Dependent Variable: Financial Performance

The R-square outcomes of 0.414 from the model in Table 3 indicated that over 41.4% of the variability of the dependent variable could be explained by the independent variables. The R-square results showed that the model was a good fit.

Table 4: ANOVA Table

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	7.291	4	1.823	11.500	.000[b]
	Residual	10.302	65	.158		
	Total	**17.593**	**69**			

a. Dependent Variable: Financial Performance
b. Predictors: (Constant), Investment Diversification in real estate, Moderated Investment Diversification in real estate

The significant F test results of 0.000 in Table 4 indicated that the model was fit and statistically significant, thus paving way for the successful running of the regression model.

Table 5: Regression Coefficients for the Direct Relationship Model

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	3.969	.639		6.212	.000
	Investment diversification in real estate	.411	.100	.467	4.123	.000

Out of the findings in Table 5, the simple linear regression model for the direct relationship model was fitted as shown in equation 4

$Y= 3.969 + 0.411X_1$ ……..……...…Equation 4

Where,

Y: is the financial performance

X_1: is investment diversification in equities

Table 6: Regression Coefficients Results for the Moderated Relationship Model

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.677	.967		2.767	.007
	Moderated investment diversification in real estate	.328	.075	.580	4.383	.000

a. Dependent Variable: Financial Performance

Out of the findings in Table 6, the multiple linear regression model for the moderated relationship model was fitted as shown in equation 5

$Y= 2.677 + 0.328_{1Z}X_1*Z$ ……...Equation 5

Where,

Y: is the financial performance

$_{1Z}X_1$*Z: is the moderated investment diversification in equities

Hypothesis Testing

The first hypothesis (H_{01}) was set as follows: Investment diversification in real estate has no significant effect on the financial performance of retirement benefits schemes in Kenya. to test H_{01}, the regression coefficients generated in table 5 were used at significant threshold of 0.05. The p value of .000 in Table 5 which was less than 0.05 informed the rejection of H_{01}, thus confirming that investment diversification in real estate has a significant effect on the financial performance of retirement benefits schemes in Kenya.

To test for H_{02}, the hypothesis for the moderating hypothesis was set as follows: **H_{02}**: Foreign Exchange rate has no significant moderating effect on the relationship between Investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya. The regression statistics in Table 6 were used to test for H_{02} at 0.05 level of significance. The p value of .000 in Table 6 informed the rejection of H_{02}, thus confirming that Foreign Exchange rate has a significant moderating effect on the relationship between Investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya. The entire summary for the hypothesis testing in this study was given in Table 7.

Table 7: Hypothesis Testing

Hypothesis Statement	P-value	Decision Rule
H_{01}: Investment diversification in real estate has no significant effect on the financial performance of retirement benefits schemes in Kenya	.000	Reject **H_{01}**, Since P-value <0.05
H_{02}: Foreign Exchange rate has no significant moderating effect on the relationship between Investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya	.000	Reject **H_{02}**, Since P-value <0.05

Discussion

The hypothesis testing in table 7 lead to the rejection of **H_{01}**, since the P-value of 0.000 was <0.05. The rejection of **H_{01}** showcased that investment diversification in real estate has a significant positive effect on the financial performance of the retirement benefits schemes in Kenya. These finding were similar to the outcomes of Makau and Jagongo (2018) who reported a significant positive effect on invetment portfolio diversification in real estate and the finanical performance of investment companies listed at the NSE. Analogous outcomes were reported by Kioko and Ochieng (2020) in their research on investment diversification and financial performance. Similar findings were reported by Muthui and Wephukulu (2019) who reported that investment diversification in real estate has a signifcant positive effect on financial performance in their study on investment porfolio diversification and financial performance.

The hypothesis testing in table 7 reported a P value of 0.000 which was < 0.05, thus resulting to the rejection of the **H_{02}**. The rejection of **H_{02}** indicated that foreign exchange rate has a

significant positive moderating effect on the relationship between investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya. Similar outcomes were reported by Kiboi and Bosire (2022) in their study on investments portfolio diversification and the financial pefromance of investment companies operating at the NSE.

CONCLUSION AND RECOMMENDATIONS

With reference to the main objective, the researcher concluded that investment diversification in real estate has a significant positive effect on the financial performance of retirement benefits schemes in Kenya. With reference to the moderating effect of the foreign exchange rate on the relationship between investment diversification in real estate and the financial performance of retirement benefits schemes in Kenya, the researcher gave the following conclusion. The researcher concluded that foreign exchange rate has a significant positive moderating effect on the relationship between investment diversification in real estate and the financial performance of the retirement benefits schemes in Kenya.

The researcher therefore, recommends that the retirement benefits schemes should consider diversifying their investments in real estate because it affects their financial performance. The researcher also recommends that the schemes should be vigilant on the volatility of the foreign exchange rate because it has a moderating effect on the relationship between the investment diversification real estate and their financial performance. In the same endeavor, the research recommends that policy formulating and regulatory bodies such as the ministry of finance, the Retirement Benefits Authority (RBA), the Central bank of Kenya (CBK), the Kenya National Bureau of Statistics (KNBS) as well as the Capital Market Authority (CMA) should devise mechanisms which ensures a close monitoring of the foreign exchange rate as well as the entire macro-economic variable volatility so as to mitigate adverse effect on the financial performance of entities.

This current study only focused at the retirement benefits scheme sector of the Kenyan economy, therefore, for further study, another study maybe conducted by incorporating other sectors of the economy, such as the banking industry and the manufacturing companies. Future studies may also incorporate other moderating variables such as the interest rate volatility as well as the consumer price index.

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