INFLUENCE OF STRATEGIC RISKS MANAGEMENT STRATEGY ON GROWTH OF REAL ESTATE SECTOR IN KENYA

Kevin Mburu Kuria
Jomo Kenyatta University of Agriculture and Technology (JKUAT)

Dr. Frida Simba
Jomo Kenyatta University of Agriculture and Technology (JKUAT)

Dr. Ahmed Anwar
Jomo Kenyatta University of Agriculture and Technology (JKUAT)


ABSTRACT

The purpose of this study was to establish the influence of strategic risk management strategy on the growth of real estate sector in Kenya. This study adopted a positivist philosophy as it aimed at testing hypotheses derived from a predetermined conceptual framework. This research used a quantitative cross sectional survey research design as the design provided accurate means of assessing information that captures respondents’ similarities and differences. The study sample comprised of all real estate firms registered by Kenya Property Developers Association (KPDA) which are 69 in number, thus a census. Primary data was gathered by use of structured questionnaires and captured through a 5-point type likert scale questionnaire. Descriptive statistics including the mean and standard deviation was used to capture the characteristics of the variables under study. Inferential statistics included use of correlation and regression analysis. Multiple regression analysis was used to establish the nature and magnitude of the relationships between the variables and to test the hypothesized relationships. All the analysis was done using SPSS statistical package. The results of data analysis were presented using figures and tables for easy understanding and interpretation. The findings indicated real estate firms had put in place several strategic management measures to promote growth. These included the existence of a board with the skills and ability to lead the firm strategically. Additionally, the board members roles extended beyond governance and into management of the firm and the board had policies stipulating term limits and rotation for its members. The study concluded that real estate sector had effective strategic risk management strategies that promoted growth and enabled effective management of reputational and governance risks. The study recommends that strict adherence to strategic risk management practices this is by ensuring that there is transparent and accountable leadership in the organization which sets the organization’s mission and vision and makes sure that the plan is followed to the latter so as to achieve the organizational goals and objectives.

Key Words: Strategic Risk Management, Strategy, Growth, Real Estate,
1. Introduction

Risk management is not a new concept in Kenya, however the development to ERM, and addressing risk beyond the traditional financial aspects, is still considered weak (Yegon, Mouni & Wanjau, 2014). The financial sector in Kenya is perhaps the leader in the development and introduction of ERM into company profiles. This is understandable given the high-risk posed by government debt, consumer spending, employment levels, fluctuating commodity prices, security threats (regional, national, and international), and reduced investments resulting from the global credit crisis. However what this list does highlight is the risk posed to the business community as a whole by these factors. Whilst it is the financial sector looking to the future, many industries are addressing the status quo without managing risks effectively and not looking to the future and how the geographical, political, and financial future of Kenya in the global market place may be affected (PWC, 2012).

A brief look at the security of Kenya’s geographical region shows the insecurity that exists and the significant effect that acts of terrorism and crime can have on the economy. The Kenyan tourism sector is an example of an industry that has been directly affected by incidents that were not necessarily directed at the sector (security and terrorism). Traditional risk management processes would not have addressed this issue, as it is not an issue seen to directly affect the sector. However, the process of ERM would have allowed for the impacts of possible national security breaches to be highlighted and thus have allowed the industry to put in place a plan of action.

Currently in Kenya, the concept of ERM is in its infancy and is dominated by multinational corporations and the financial industry (Deloitte, 2012). Although the concept of Risk Management is present throughout most industries, the process is limited in most cases to just the financial aspects of organisations. This status quo has served the corporate sector well in the past economic climate, but the increase in globalisation has meant that even regional economies have to be aware of the far reaching effects posed by international events.

Several failures of large firms, increase in technology impacting the ability to track firm risks, and increases in regulatory scrutiny of managers and directors has led to the progression of ERM. The collapse and failure of business has forced businesses to place more focus on the management of
risks relating to all aspects of their businesses. This management therefore incorporates use of ERM which describes the set of activities that businesses undertake to deal with all the diverse risks that face it in a holistic/strategic/integrated method such as financial, strategic, operational, hazardous, and compliance risks, spanning through the organization. Many of such risks have significant impact on the profitability, effectiveness, and reputation of business enterprises. The growth of ERM has also led to increased interest among academic researchers examining firm performance and firm value. Additionally, risk managers, ratings agencies, regulators, and investors are becoming more interested in ERM and its impact on firms (Gates, 2006).

The economic and business planning framework and priorities have shifted from the short term and tactical to the long-term and strategic (Betts & Ofori, 2002), due to various factors including the particular challenges of the business environment (Benjamin, Rockart, Morton & Wyman, 2004) caused by the increasing global competition in various industries (Levit, 2003). Strategic management practice is an important practice as it gives a strong influence towards firms’ success. The importance of strategic management in a firm can be answered by looking at the relationship between strategic management and organizational performance. Strategic management does give positive influence, especially in its profitability to the large firms (David, 2007).

Although it has been demonstrated that strategy management can improve business performance, it has also been acknowledged that environmental uncertainties might affect the postulated relationship (Day & Wensley, 2008; Kohli & Jaworski, 2010). Carpano, Chrisman, and Roth (2004) stated that, depending on the competitive situation that firm’s face, the performance of firms following a particular strategy can vary. Others have added that, in certain environments, certain strategies would lead to significantly higher performance than other strategies (Belderbos & Sleuwaegen, 2005; Williamson, Jenkins, Cooke, & Moreton, 2004). The recession has forced businesses to place more focus on the management of risks relating to all aspects of their businesses. Such management is broadly defined as Enterprise Risk Management, which describes the set of activities that businesses undertake to deal with all the diverse risks that face it in a holistic/strategic/integrated method. These risks include financial, strategic, operational, hazardous, and compliance risks, spanning through the organization. Many of such risks have significant impact on the profitability, effectiveness, and reputation of business enterprises (Society of Actuaries [SOA], 2009).
The housing sector has a critical role to play in the achievement of the goals envisaged by Vision 2030. Housing construction is a labour-intensive activity that will create jobs for youth and the unemployed. Construction also has strong linkages with other sectors of the economy. Proper planning and effective management of and increased investment in our urban areas are critical for the realisation of this objective. The housing sector is one of the principal levers for creating jobs among the youth, driving economic growth, and tapping the opportunities in linkages with other sectors. The housing sector has a local content of more than 90 per cent, implying that investment in housing and integrated planning will have direct positive effects on the national income by triggering forward and backward linkages through additional investments in manufacturing of building materials, transport, marketing and infrastructure development.

Changes in the internal and external environment of business have heightened interest in centralized risk management. A holistic approach to risk management is believed to be more effective than traditional silo approaches, particularly for firms faced with increasingly complex and interrelated risks. In the last decade, large firms have increasingly adopted enterprise-wide approaches for dealing with the wide variety of risks they face (Beasley et al., 2012). In a well designed enterprise risk management (ERM) program, the firm integrates risk management into the strategic planning process, addressing strategic, financial, operational, and hazard risks under a single overarching process (Hoyt and Liebenberg, 2011; Ai et al., 2012; Grace et al., 2014). This is in contrast to more traditional silo approaches to risk management in which each type of risk is managed separately. Industry and rating agencies report anecdotal evidence that ERM softened the effect of the economic recession, increasing adopting firms’ identification of and preparation for complex and interrelated risks (S&P, 2012). This study therefore seeks to establish the effect of strategic risk management strategy on the growth of real estate firms in Kenya.

2. Statement of the Problem

The real estate industry must be supported and it will have to grow at a faster pace than it currently does. The Kenya industry is benefiting from economic growth of the country and the inflow of foreign aid is being regarded as a very promising venture. The government is also heavily investing in this industry in various ways such as the inclusion of the ministry of housing in the government
body, availing of funds to the housing ministry; enforcement of laws to do urban planning, regulatory laws in license permits (Homes Expo Kenya, 2012)

Given the ever dynamic and challenging business environment, real estate sector is bound to be exposed to various risks. The problem is that real estate companies that do not adapt and/or institutionalize ERM strategies are likely to witness poor growth patterns compared with those that adapt ERM. The poor growth or failure of the real estate sector may lead to serious negative consequences as far as the achievement of Vision 2030 is concerned owing to the important role real estate companies are expected to play in providing affordable housing for citizens.

Following several discussion papers on ERM and empirical studies that examined firm characteristics related to ERM, researchers began asking how ERM affects firm value. Although the findings are mixed for this question, many authors hypothesize that ERM adds value through increased efficiency in the risk management process, better communication across departments related to risk decisions, and improved risk quantification.

Nocco and Stultz (2006) argued that ERM adds value to firms because it enables risk quantification and optimization by managers so that the firm can choose the best operating strategy and that ERM should integrate with a firm’s culture and incentivize workers to make decisions that align with firm objectives. Additionally, because ERM considers all risks simultaneously, it can be a useful tool in determining the optimal level of default risk (Nocco & Stulz, 2006).

Mackay and Moeller (2007) tested the value of firms that used corporate risk management. They found that corporate risk management leads to an increase in value for a corporation when risk factors are not linearly related to revenues and costs. This finding differs from some prior studies, which showed a weak or negative relationship between risk management and firm value (Tufano, 2006). Mackay and Moeller (2007)’s finding of a positive relation between risk management and value may be due to greater efficiency in risk management and firm communication regarding risk practices (Hoyt & Liebenberg, 2011).

Kinyua (2010) assessed risk as a component of corporate strategy in selected life insurance companies in Kenya and found out that insurance companies faced competitor, regulation and de-regulation risk and industry economics and recommended that insurance companies should deploy...
strategic planning tools to give the firms an all-inclusive perspective of strategic planning. Njoroge (2013) also conducted a research on the strategic risk management practices by AAR Insurance Kenya Limited showed that reputational risk is significant in insurance companies. This study sought to establish the influence of strategic risk management on the growth of real estate sector in Kenya.

3. Purpose of the Paper

The purpose of this study was to establish the influence of strategic risk management strategy on the growth of real estate sector in Kenya.

4. Literature Review

4.1 Strategic Risk Management Strategies

Slywotzky and Drzik (2005) defined strategic risk as the array of external events and trends that can devastate a company’s growth trajectory and shareholder value. While these two authors consider strategic risk as a sole consequence of external occurrences, other authors look at strategic risk as the current and prospective impact on earnings and/or capital arising from internal business activities such as adverse business decisions, improper implementation of decisions, or lack of responsiveness to industry changes. Thus consider strategic risk as a function of the compatibility of an organization’s strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals, and the quality of implementation. Emblemsvåg and Kjølstad (2002), also defined strategic risk as risk which arises as a firm pursues its business objectives either by exploiting opportunities and/or reducing threats.

Strategic risk encompasses a variety of uncertainties which are not financial in nature, but rather credit or operational related caused by macro-economic factors, industry trends or lapses in a firm’s strategic choices which affects the firm’s earnings and shareholders’ value adversely. Strategic risks often constitute some of a firm’s biggest exposures and therefore can be a more serious cause of value destruction. Unfortunately, as strategic risks are often highly unpredictable and of different forms, managers have also not yet been able to systematically develop tools and techniques to address them (Slywotzky & Drzik, 2005).
Njoroge (2013) studied the strategic risk management practices by AAR Insurance. Identified reputation risk as the most significant risk facing the company. This study employed case study research design. The target population comprised of 40 senior management and middle level staff at AAR Insurance Kenya Limited drawn from the department of finance, underwriting and operation. The study recommended that the Board should continue taking ownership and driving the risk agenda across the business. It was also recommended that the organization should focus on new emerging risk types such as reputation, operational risks and IT security while not losing focus on the traditional risks such as credit and market risks. AAR should also define risk management framework and program which enables effective reporting and consolidation of data.

5. Methodology

This study used a correlational survey research design. A survey research design is an attempt to collect data from the members of a population in order to determine the current status of that population with respect to one or more variables. The choice of correlational survey research design was because it is used to explore relationships between variables and to predict a subject score on one variable on given his or her score on another variable. This method permits one to analyze interrelationships among a large number of variables in a single study. It also allows one to analyze how several variables either singly or in combination might affect a particular phenomenon being studied. The method also provided information concerning the degree of relationships between the variables being studied. Reviewed studies, for instance, Tseng (2007), Hoyt and Liepenberg (2010) used correlational survey research design in their attempt to link ERM strategies to performance of firms.

The target population was the management employees of real estate firms, registered under the (KPDA) in Kenya. According to the Kenya Property Developers Association, the estimated number of real estate firms as at close of 2012 was 69 firms spread across the country. The study used purposive or convenient sampling technique. The sample size for this study was 276 employees who were obtained by purposively selecting four respondents from the 69 real estate developers who included the operations manager, finance managers, real estate portfolio manager and property development manager. The study used primary data specifically a structured questionnaire to collect data. Data was collected, coded and analyzed using SPSS version 20.0.
The findings were presented in form of tables and pie charts and discussions and interpretation of the same given.

**6. Results and Discussions**

**6.1. Response Rate**

The number of questionnaires, administered to all the respondents, was 276. A total of 216 questionnaires were properly filled and returned from the real estate in Kenya. This represented an overall successful response rate of 78%. According to Mugenda and Mugenda (2003), a response rate of 50% or more is adequate. Babbie (2004) also asserted that return rates of 50% are acceptable to analyze and publish, 60% is good and 70% is very good. Therefore, a 78% response rate from this study is considered to be very good and satisfactory hence it was appropriate for this study.

**6.2. Descriptive Statistics**

The fourth and the last objective of the study sought to establish whether reputational/strategic risks management strategy contributes to growth of real estate sector in Kenya. Results in Table 4.22 shows that 86.1% of the respondents agreed that the board had the skills and ability to lead the firm strategically, 81.5% agreed that the board members’ roles extend beyond governance and into management of the firm and 71.3% agreed that all board members agreed on the firm’s mission and strategic direction. Seventy seven point seven (77.7) percent of the respondents agreed that the management ensured utilization of appropriate building materials and low-cost construction technologies, 68% agreed that there was a strategic plan in place to mitigate or handle any business risks that may arise and 72.3% agreed that the board had set up various committees to oversee the firms projects.

In addition, 73.6% of the respondents agreed that the board had policies stipulating term limits and rotation for its members, 67.6% agreed that the firm had guidelines preventing conflicts of interest among board members and 79.2% agreed that the organizational structure ensured staff accountability. Finally, 82.9% of the respondents agreed that the organizational structure enhanced the firm’s efficiency and productivity and 75% agreed that the organizational structure supported effective management oversight. The mean score for the responses was 3.94 which indicates that
majority of the respondents agreed that strategic risk management strategy influenced growth of real estate firms in Kenya positively.

The findings are in line with Njoroge (2013) who studied the strategic risk management practices by AAR Insurance and identified reputation risk as the most significant risk facing the company. The study recommended that the Board should continue taking ownership and driving the risk agenda across the business. It was also recommended that the organization should focus on new emerging risk types such as reputation, operational risks and IT security while not losing focus on the traditional risks such as credit and market risks.

6.3. Regression Analysis

Regression analysis was conducted to empirically determine whether strategic risk management strategy was a significant determinant of growth of real estate sector in Kenya. Regression results in Table 1 indicate the goodness of fit for the regression between strategic risk management and growth was satisfactory. An R squared of 0.435 indicates that 43.5% of the variations in growth are explained by the variance in strategic risk management strategies employed by real estate firms. This implies that 56.5% of the unexplained variations in growth is accounted for by the other variables including credit risk management, operations risk management and regulatory risk management strategies.

Table 1: Model Summary for Strategic Risk Management Strategies

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.659a</td>
<td>0.435</td>
<td>0.432</td>
<td>0.62805</td>
</tr>
</tbody>
</table>

a Predictors: (Constant), StrategicRiskMgt

F-test was carried out to test the null hypothesis that there is no relationship between strategic risk management strategies and growth of real estate sector. The overall model significance was presented in table 2 and shows that the F statistic is 164.558 with a P-value of 0.0000 which implies that the regression model is significant. Therefore meaning that null hypothesis is rejected and alternative accepted concluding that there is a relationship between strategic risk management
strategies and growth of real estate sector and thus strategic risk management strategies were statistically significant in explaining growth of real estate in Kenya.

**Table 2: Goodness of Fit Model of Strategic Risk Management on Growth**

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>64.91</td>
<td>1</td>
<td>64.91</td>
<td>164.558</td>
<td>.000b</td>
</tr>
<tr>
<td>Residual</td>
<td>84.412</td>
<td>214</td>
<td>0.394</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>149.322</td>
<td>215</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a Dependent Variable: Growth  
b Predictors: (Constant), Strategic Risk Mgt

The results of regression analysis as presented in the Table 3 below, shows that strategic risk management strategies by real estate sector has a positive significant effect ($\beta=0.736$, P-value =0.000) on growth of real estate. The results show that strategic risk management strategies contribute significantly to the model since the p-values for the constant and gradient are less than 0.05. The findings imply that one positive unit change in strategic risk management strategies effectiveness led to a change in growth of real estate at the rate of 73.6%. This confirms the positive effect of strategic risk management strategies on growth of real estate in Kenya. Results are in consistent with those of Njoroge (2013) who conducted a research on the strategic risk management practices by AAR Insurance Kenya Limited showed that reputational risk is significant in insurance companies.

The regression equation obtained from this output is:-

Growth = 0.996 + 0.736 Strategic Risk Management Strategies
Table 3: Coefficients for Strategic Risk Management Strategies

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 Constant</td>
<td>0.996</td>
<td>0.228</td>
<td></td>
<td>4.374</td>
</tr>
<tr>
<td>Strategic Risk Mgt</td>
<td>0.736</td>
<td>0.057</td>
<td>0.659</td>
<td>12.828</td>
</tr>
</tbody>
</table>

a Dependent Variable: Growth

7. Conclusions and Recommendations

Strategic risk management strategies were found to have a positive and significant effect on growth. The study concluded that real estate sector had effective strategic risk management strategies that promoted growth and enabled effective management of reputational and governance risks. This was enhanced by the measures put in place by the firms such as the organizations constituted boards with the skills and ability to lead them strategically, the board members roles extended beyond governance and into management of the firm, the board had policies stipulating term limits and rotation for its members, utilization of appropriate building materials and low-cost construction technologies, use of a strategic plan to mitigate or handle any business risks that may arise and setting up various committees to oversee the firm’s projects. The findings also led to the conclusion that the board members agreed on the firm’s mission and strategic direction which ensured that all the employees worked towards achievement of the set organizational goals and objectives. The study also concludes that the organizational structure ensured staff accountability and enhanced firms efficiency and productivity which were attributed to by having a workable strategic plan that has been drafted with all parties involved.

The study recommends that strict adherence to strategic risk management practices this is by ensuring that there is transparent and accountable leadership in the organization which sets the organization’s mission and vision and makes sure that the plan is followed to the latter so as to achieve the organizational goals and objectives. The management should therefore be committed to the formulation of strategic plans for the organization showing the direction the company will take in achieving the short and long term goals.
References


