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ENVIRONMENTAL MUNIFICENCE AND PERFORMANCE OF INSURANCE COMPANIES IN KENYA

JOHN MUTUGI GACHOKI
Kiriri Women University of Scince and Technology
Mobile: 0704 689 561

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ABSTRACT

In the last 5 years, the Kenyan economy has been experiencing turbulence and the market has been unstable for business. Some businesses have reported losses, others gone under while majority are barely surviving on government aid. This is partly attributed to the prolonged drought, insufficient rainfall, Covid 19 pandemic, Russia-Ukraine war and the long 2022 campaign period for 2022 general elections. The insurance industry has been hard hit considering majority of Kenyans consider insurance as secondary service. This implies that any reduction in their disposable income reduces their chances of acquiring an insurance cover. This study therefore sought to find out the effect of environmental munificence on performance of insurance companies in Kenya. The indicators for environmental munificence were market share, market orientation and sales growth. Performance of insurance companies was measured through analyzing the return on equity. All the 55 registered and licensed insurance companies in Kenya were considered for this study. A regression model was used to test the relationship among the interacting variables. Environmental munificence was found to have a negative significant effect on equity. During the period under review, market share and sales indicated a negative effect on return on equity while market orientation had insignificant statistical results. This study concluded that improvement in environmental munificence results to increase in return on asset while a decline in environmental munificence results into negative results. This study recommends that insurance companies should first study the environment to determine whether its munificence or not before introducing products or services to the economy. The findings of this study will be helpful to students and scholars, business's particularly insurance companies and the government.

1.0 INTRODUCTION

The environment in which business organizations operate is a complex, multi-focus dynamic and has a far-reaching effect on such organization. In management, the word "Environment" does not necessarily mean physical surroundings, but is used to describe all those influences that bear upon the individual organizations and affects the decisions, strategies, process and performance of the business. (Baloch, Maher & Khan,.2021). Many organizations according to the contingency theory, pursue a fit between their structure and the environment (Rasche, 2008). This fit and adaptation depends to a certain level on environmental determinism (Rabetino et al., 2021). Business environment in which organizations operate were found by Kinuu, (2014) to exerts pressure on them provoking different responses as they seek legitimacy to survive and prosper in their environment. Given by the interaction between organizations and environment. Feng et al. (2017), asserted that performance relates to how an organization reacts, understands and influence to certain environment changes.

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Munificence, in general, refers to an environment's ability to support sustained growth of an organization (Aldrich, 1979). Studies previously done on a similar scope yielded contradictory and inconclusive results which led to disagreement as to whether environmental munificence improves or reduces performance. The more munificent the environment is Chakrabarty & Wang, (2012), observed that the more options the companies have because alternative goals, strategies and organizational structures become possible to pursue. Farooq (2017) found that environmental munificence to not only buffers organizations from environmental pressures by generating financial slack but also allow firms an opportunity to adjust or balance in response to the environment. Further, Beliaeva et al. (2018) observed that munificence increases the opportunities for performance by providing many growth opportunities which can reduce the perceived challenges associated with multiple channels serving the same market. Consequently, yuan et al, (2019) noted that salespeople working in an environment with high munificence may anticipate higher sales growth.

In hostile or non-munificent environments, Gorondutse and Hilman (2017) observed that scarcity of resources forces firms to pay greater attention to their conservation. Under conditions of environmental scarcity Feng et al (2016) observed that perceptions of high levels of constraints and competitive pressures may precipitate a crisis-like. Staw and Swajkowski (1975) found that firms in non-munificent environments are more likely to commit illegal acts while economy Akinmulegun and Oluwole, (2013) evidenced that non-munificent environments intensified competition, rigidity of response, and fewer strategic options. Further, efficiency concerns arose in scarce environments manifested in the tightening of budgets, increased emphasis of cost cutting, and intensification of efforts to ensure accountability which resulted in negative performance.

Inferring from the confusion brought by the contradicting results of different researchers, this study seeks to clear the dust though determining the effect of environmental munificence on performance evidenced by data from the Kenyan insurance sector. Findings of this study informs on the current status of insurance industry in Kenya and among African countries. Second, the study forms part of a body of knowledge to the scholars in the academia and service industry and provides insight on the concepts of cannibalization and how they influence performance. Further, the study was undertaken in Kenya, a developing country thus findings of this study could be related to other developing countries. This study also forms an invaluable source of reference especially when developing policy guidelines for the insurance sector. The owners and management of insurance companies benefit from this study through gaining more insights concerning the effect of environmental munificence to performance.

2.0 BACKGROUND OF THE STUDY

The Kenyan insurance industry asset base has continued to grow over the last five years. IRA (2020) reported that the insurance industry assets as at the end of 2020 amounted to KES 765.93 billion, a growth of 8.0% from KES 709.05 billion reported in 2019. In the year 2017, the industry adopted a new strategy of developing and disseminating information education through insurance training champions, mobile clinics and other outreach activities conducted by the Authority (IRA 2017). Over the year's, continuous development has been initiated in the insurance sector including educating the public through television and local radio stations (AKI, 2021). This was aimed at enhancing insurance awareness levels, increasing the uptake

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of insurance products and the ultimate expectation was that it lead to increased insurance performance. Today's insurers are being compelled by their existing and new competitors to deliver new offerings to meet consumer needs, preferences and market dynamics that continue to evolve at an accelerated rate. With other industries placing the customer at the center of their businesses, insurers are still lagging behind with most continuing with a product-push approach. Further the industry asset base increased from assets worth ksh 528,748,193 in 2016 to assets worth ksh 765,932,479 in 2020.During the same period shareholders increased their investments from ksh 134,482,581 in 2016 to ksh 166,069 303(IRA; 2016,2020). Despite the positive developments in the insurance sector, the industry performance is on a negative trend.

The returns on equity have been on a downward trend despite consistent year-on-year increase in shareholders' funds (IRA, 2021). Insurance penetration, which is the ratio of gross direct insurance premiums to gross domestic product has been declining from 2.81% in 2016 to 2.57% in 2017 to 2.43% in 2018 to 2.37% in 2019 to 2.30% in the year 2020. (IRA;2016,2017,2018,2019,2020). In the year 2020, association of Kenyan insurers observed that 254,764 new policies were underwritten which was a decrease of 10.8% from 285,725 new policies recorded in the previous year (AKI, 2020). Further examinations of the insurance industry reports revealed that Profit after tax reduced by 68.64% from KES 12.71 Billion in 2019 to KES 3.99 Billion in 2020.

3.0 THEORETICAL FRAMEWORK

3.1 Institutional theory

Institutional theory was introduced in the late 1970s by John Meyer and Brian Rowan as a means to explore further how organizations fit with, are related to, and were shaped by their societal, state, national, and global environments (David ,2012). Institutional theory gives us a way to understand how organizations might navigate rules and norms of the system in order to appear legitimate and survive (Pontikes & Kim 2017). Further the theory suggests that individuals, organizations and groups behave in ways, which reflect the normative, political, cognitive and regulatory rules of their institutional environments, adherence to which warrants legitimacy (Canales ,2016). As a result, Besharov & Smith (2014) found it possible to broadly classify institutions as formal and informal ones and confirmed that both must conform to their environment else they perish. Consequently, Mair., Mayer, & Lutz, (2015) noted that institutions provide the rules of the game that shape the human interactions in the societies they are part of. This theory relates to this study in the respect that insurance companies operate in environments that are increasingly uncertain, complex, competitive, dynamic and unpredictable. Cassandra & Bradley, (2016) further noted that this changes in environment are not only rapid and bewildering but also in a state of constant flux. Institutional theory is employed in this study to explain how munificence of the environment influences performance of insurance company in Kenya.

3.2 Contingency Theory

Contingency is a philosophical notion defined as the possibility that something happens or does not happen. It is, in other words, a random event (Tangpong, Hung & Li J 2019). contingency theory, explains how external conditions correlate with organization's internal structure to form

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an organizational fit that determines their performance. The origins of this theory can be traced back to the works of prominent scholars such as Donaldson (1987), Drazin and Van de Ven (1985), Thompson (1967), and Venkatraman (1989). The theory upholds the belief that there is "no one best way" of managing or organizing but it depends on the "fit" between the organization and the environment (Boso et al. 2013). Further McAdam et al., (2019) contend that theories of contingency consider that the structure of an organization depends both on its own characteristics and on the environment in which it operates. However, Gualandris and Kalchschmidt (2016) found that any efficient structure must adapt to the environment on which it depends, which makes factors contingencies internal or external to the company, which will influence its structure in a decisive way. Findings of Agrawal, (2014) revealed that situational factors can affect the relationships between dependent and independent variables in the work environment, which in turn will affect employee behavior, motivation, and effectiveness affecting the overall performance. Conclusions made by Pratono, (2016) supported contingency theory through affirmation that organizations whose internal features best matched the demands of their environments achieved the best adaptation. In the context of this study, external pressures in the form of social relationship, global pandemic, government policies and technological dynamic are seen to be the environmental factors that influence performance

4.0 EMPIRICAL REVIEW AND HYPOTHESIS DEVELOPMENT

4.1 Environmental Munificence

Environmental munificence is defined by Tan (1996, in El - Nadi, 2013) as "the level of resources available to firms from various sources of the environment". Institutional theory postulate that business environment in which organizations operate exerts pressure on them provoking different responses as organizations seek legitimacy in order to survive and prosper in their environment (Kinuu, 2014). The more munificent the environment is; the more options companies have because alternative goals, strategies and organizational structures become possible to pursue (Chakrabarty & Wang, 2012). Environmental munificence as observed by Farooq (2017) not only buffers organizations from environmental pressures by generating financial slack but also allow firms an opportunity to adjust or balance in response to the environment. Further, Gorondutse and Hilman (2017), observed that munificent environments impose fewer constraints on organizations than do those environments with resource constraints. Findings Meinhardt et al., (2018) showed that a highly munificent or resource-abundant environment enables a firm to focus less on its primary goal of survival, because survival is possible under a variety of alternative goals, strategies, and configurations. Such an environment was observed by Porto et al. (2009) to presents minimal competitive pressure and offers maximal strategic options and relative harmony among organizational constituencies. A study done by Jaiyeoba (2013) concluded that resources available within an environment influenced the survival and growth of firms sharing that environment and also affected the abilities of new firms to enter that environment.

In non-munificent environments, because companies are already short of resources, Olaru and Purchase (2015), found that deployment of any resources away from core market areas is likely to have no positive effect on performance. Further, in hostile or non-munificent environments, Li et al (2013) established that the scarcity of resources forces firms to pay greater attention to their conservation and are more likely to commit illegal acts. Gualandris (2016) found that

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variations in socio-economic, cultural, and governmental conditions influence the way individuals evaluate opportunities which, in turn, affects their tendency to stay on the lookout for new business opportunities. Consequently, entrepreneurs in a highly munificent environment that provides abundant financial as well as non-financial resources are expected to differ in their alertness levels from entrepreneurs in low munificent environment in which they are more likely to encounter difficulties.

Elaborating on the construct of munificence, Bagire and Namada (2013) identified three distinct kinds of munificence: capacity, growth/decline, and opportunity/threat. Capacity refers to the level of resources available to the firm, growth/decline refers to the change in capacity, and opportunity/threat refers to the extent of unexploited capacity. In general, LI et al. (2013) found that growth and/or decline dimension that was signified by characteristics such as market share gains, growth in demand, and sales growth was a much better predictor of performance than the opportunity and/or threat dimension characterized by a firm's ability to handle competitive moves, changing customer preferences, and the ability to retain employees. Feng et al. (2017) state that a firm's environment and the fit between the environment and firm's capabilities are significant in determining the returns to its capability investments. In munificent environments Agrawal (2014) established that costs of errors associated with relatively lose control of operations seem negligible compared to the benefits of opportunities created through rapid removal of constraints and timely responses to competitive pressures.

H1. Environmental munificence has a significant effect on performance of insurance companies in Kenya.

5.0 METHODOLOGY

5.1 Research Design and Sample Size

This study employed causal comparative research design. Causal comparative design was appropriate for this study hence employed as ex-post-facto since the alleged cause and effect had already occurred (Frank & Rens, 2017; Richardson, 2018). The study employed data from audited annual financial statements from all 55 insurance companies in Kenya that had the data for 5 years starting from the year 2017 to 2021.

5.2 Operationalization and Measurement of Variables

Findings of LI et al. (2013) established environmental munificence was better predicted by considering the growth and/or decline dimension. that was signified by characteristics such as market share gains, growth in demand, and sales growth. The effects of market munificence was further measured using the average scale as given by Li and Greenwood (2010).

$$\text{Sales growth} = \frac{\text{current}-\text{past}}{\text{past}} \text{x}100 \quad \ldots\ldots (1)$$

$$\text{customer growth} = \frac{current-past}{past} x100 \quad \ldots\ldots (2)$$

$$\text{market share} = \frac{total\ brand\ purchase}{total\ category\ purchase} \quad \ldots\ldots (3)$$

The factor scores that emerged from the confirmatory factor analysis represented environmental munificence if the results were positive while if the results were negative then it suggested decline or non-munificent environment.

5.3 Research Model

The theory of production was applied to model the study. The theory of production dates back to Adam Smith who laid the foundations of the factors of production (Smith, 1776) who observed production as a process of combining various material inputs and immaterial inputs (plans, know-how) in order to make something (output) (Kotler et al., 2006). This study thus seeks to extend the knowledge by using the Cobb–Douglas production and its application in the insurance sector.

Cobb–Douglas production function in the form of $Y=AL\alpha K\beta$ was adopted where Y, L and K represented product quantity, labor and capital respectively. A represented the level of technology adopted and the associated output elasticities were represented by α and β. The Cobb–Douglas production function was linearized to fit in the study for estimation. Therefore, the following model was obtained;

$LogY = logA + \alpha Log\ L + \beta LogK + u$ …….……. (4)

To align the model with the study variables, having used a panel data set for N firms observed for T periods, the model was further modified as follows;

$Yit = ait + \lambda ixit + uit$……..…… (5)

Where Yit was performance of firm i at time t, Xit was a vector of predictor variables, λi was the elasticity of predictor variables and Uit was the error term.

To test the study hypothesis, equation 2 was further improved to;

$Yit=Bo+BiSGit+B2CCit+B3MSit+eit$…….…… (6)

Where Y was performance of an insurance company, SG sales growth, CC was change in customer, MS was market share, i was the specific company and t was a specific time period.

6.0 RESULTS AND DISCUSSION

6.1 Descriptive Statistics

The descriptive statistics results are presented below.

Table 4.1: Descriptive Statistics

Variable	Mean	Std Dev	Min	Max
Sales growth	1.10	4.45	-2.78e	3.77e
Customer growth	29.264	419.62	-1	6167.8
Market share	0.57	0.22	0.33	1.00

ROE	-.0115	.6946	-8.126	2.235

From the table above sales growth had a mean of 1.10 with a standard deviation of 4.45 ranging from a minimum of -2.78 to a maximum of 3.77. This meant that sales growth ratio was less than 1 thus the insurance companies' sales was grown during the period under review. Customer growth exhibited a mean of 26.264 with a standard deviation of 419.62 ranging from a minimum -1 to a maximum of 6167.8. This meant that customer growth was less than 1 and thus the insurance companies gained by cannibalizing their sales done by agents from sales made by banks. Results in table 4.1 above showed that return on assets had a mean of 0.021 with a standard deviation of 0. 139.This implied that on average return on assets for insurance companies stood at 2.1% and fluctuated from a minimum of -0.958 to a maximum of 0.923. The wide range showed that return on assets was not constant but kept fluctuating over the years. Return on equity was found to have a mean of –0.011 and a standard deviation of 0.695 and it fluctuated from – 0.8.1 to 2.235 during the period under consideration.

7.0 DIAGNOSTIC TEST

7.1 Normality

Normality test is used in statistics to determine whether a set of data is modeled well by a normal distribution. (Razali & wah,2011). Analysis to assess normality of data was done using Shapiro Wilk Test.The null hypothesis was that data was normally distributed. The decision criteria were that where P value <0.05, the null hypothesis would be rejected implying that data is not normally distributed (Tabachnik & Fidell,2007).

Table 4.2: Shapiro Wilk Test Results

VARIABLE	W	V	Z	Prob>z
Sales growth	0.28199	136.623	11.471	0.0783
Customer growth	0.59753	76.581	10.121	0.122
Market share	0.05358	178.278	12.085	0.098
ROE	0.34542	112.435	10.954	0.235

Results of table 4.2 above revealed that the data normally distributed as was indicated by all the variables having a p-value above 0.05.

7.2 Hausman Test

To arrive at the best choice of the model between fixed effects and random effects Hausman test was used. The null hypothesis was that the preferred model was random effects. As suggested by Chmelarova (2007), when p-value is less than 0.05, the null hypothesis would be rejected.

Table 4.3 Hausman Test Results

DV used	Statistics	P value
Sales growth	5.42	0.436
Customer growth	1.10	0.356

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Market share	4.12	0.411
ROE	9.06	0.964

The results from the hausman test revealed that all variables had a p-value greater than 0.005 hence the study relied on a fixed effect model.

7.3 Heteroskedasticity

Heteroscedasticity test determines whether there exists an unequal spread or variance among residuals of the population of study and where the error variance is not constant, then there is presence of heteroscedasticity (Williams, 2015). The Breusch-Pagan test was used to test the null hypothesis that the variance of the residuals is homoscedastic (has a constant variance). When the P-values >0.05, the study will fail to reject the null hypothesis and presence of homoscedastic will be confirmed implying that there was no problem of heteroskedasticity (Data was homoskedastic and has a constant variance.

Table 4.4: Heteroscedasticity Test

	Sales growth	Customer growth	Market share
Variables:fitted values of ROE	22.4 (0.0000)	16.5 (0.0000)	20.4 (0.0000)

P values are enclosed in the brackets

Effect of environmental munificence on Performance

The study sought to establish the effect of environmental munificence on performance of insurance companies as measured by return on equity and return on assets.

Table 4.5: Effect of Environmental Munificence on R O E

	Coef.	Std Err	t statistic	P-value
Sales growth	-9.61e-15	8.13	-0.12	0.906
Change in customers	-.001317	.0001256	-10.49	0.000
Market share	.0012891	.0041239	0.31	0. 041

F statistic was (55.07) with a P-Value of 0.0000

Results in table 4.5 showed that F statistic (55.07) was significant at P-Value 0.0000 less than 0.05 indicating that the variables fitted well for estimation of munificence. The overall r – squared was 0.5315 indicating that 53,15% of variation in ROE was accounted for by Munificence. The correlation coefficient was 0.0022. This indicated a positive correlation between munificence and ROE. This implied that a 1% increase in Munificence would lead to an increase of ROE by 0.22%. Further, the results indicated an insignificant coefficient (-9.61e-15) of sales growth with a p-value of 0.906. This indicated that sales growth as a measure of munificence has no effect on ROE. In addition, the results show a significant negative coefficient (-0.0013) of change in customers with a p-value of 0.000. This indicated that change in customers as a measure of munificence has a negative effect on ROE. This implied that 1% increase in customer change would result to a decline in ROE by 0.13%. On market share the

study found a significant positive coefficient (0.0012) implying that market share as a measure of munificence had a positive significant effect on ROE. Further interpretation of the results shows that a 1% increase in market share would result to an increase in ROE by 0.12%.

8.0 SUMMARY OF FINDINGS

The main objective of the study was to investigate the relationship between channel Environmental Munificence and performance of insurance companies in Kenya. The study sought to determine whether the customers, market share and companies' sales were influencing performance of insurance companies. Performance was measured through focusing on return on assets and Return on equity. Data was collected from the audited and published financial reports of insurance companies for 5 years from the year 2016 to 2021. Shapiro Wilk Test Results revealed that the collected data was normally distributed. Fixed effect model was employed in this study because hausman test results produced p-values that were greater than 0.005. Further, the data was found to be homoscedastic with a constant variance as was revealed by Breusch-Pagan test results. Regression analysis was done to determine the relationship between the variables and to determine the effect of environmental munificence on Performance of the insurance companies.

This study found that sales growth as a measure of munificence had no effect on ROE. This study therefore concludes that insurance companies should not only focus on increasing sales but should lay more emphasis on the cost of sale. This is because sales growth did not account for any significant effect to the return on equity. In addition, change in customers as a measure of munificence had a negative effect on ROE. This implied that 1% increase in customer change would result to a decline in ROE by 0.13%. On market share the study found a significant positive significant effect on ROE implying that a 1% increase in market share would result to an increase in ROE by 0.12%.

9.0 CONCLUSION

Based on the finding, this study concluded that environmental munificence had significant effect on performance of insurance companies in Kenya. A positive increase in numbers of customers had positive effects on performance while a negative decrease in number of customers resulted to poor performance. Further this study concludes that when insurance companies expand their market share then the resultants outcome is increase in performance.

10.0 RECCOMENDATION

Insur Tech start-ups and companies that are completely outside the traditional insurance space are encroaching the territory which largely belonged to insurers in the past. Therefore, it is critical for insurers to upgrade their technological capabilities under the umbrella of innovation to maintain or grow their market penetration. Insurers need to move from the traditional reactive experience to a predictive and proactive experience. They will need to rethink their operating models, reimagine their workforce, and start thinking of agile ways to bring innovative products to the market. With the increasingly discerning consumer, insurers should start being aware of the potential for external market participants to encroach their market share. Consumers are looking for solutions to manage their risk in a way that is convenient to them, and insurers need to develop solutions that meet these needs instead of the traditional

product-push approach that has been successful in the past. This new type of insurance offering should be based on artificial intelligence (AI), machine learning, big data, and analytic cloud computing.

Munificence of an environment can be increased by implementing policies that will encourage financial investment and knowledge development. Customers will not be satisfied with the status quo when they only use their car for a limited time every day, or worse if they do not own a car as we see in the shared economy. They will look for better, smarter, and cheaper alternatives to the traditional annual policies. This study therefore recommends that insurance companies adopt a partial motor insurance to only cover the vehicle when only in motion or use.

To drastically improve the customer experience, this study recommends that insurance firms must therefore look at adopting technologies that make the customer's life easier, deliver results quicker and offer the ability to engage with the customer anywhere, anytime. This can either be at the new policy stage, or in policy administration during the life of the customer, or indeed in claims. Customer satisfaction should be at the top of an insurer's agenda to ensure continuity and retention of business from the customers. when considering the cost implications, a key note is that retaining existing customers is more cost effective than acquiring new customers.

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