

The Determinants Of Financial Performance Of Insurance Companies In Ethiopia

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ABSTRACT

The purpose of this study is to examine the factors that contribute to the financial performance of insurance companies in Ethiopia. The researcher used a quantitative research approach and an explanatory method of research design. The researcher analyzed secondary panel data from the period 2017-2021 for all insurance companies operating in Ethiopia. The researcher measured financial performance using the return on assets (ROA) ratio. It also investigated the relationship between independent variables such as leverage, liquidity, management competency index, investment ratio, company size, market share, inflation, and GDP growth, and the dependent variable ROA. Descriptive statistics, correlation analysis, and OLS regression analysis were performed to analyze the financial performance of insurance companies. The regression results showed that the ROA was positively and significantly influenced by the management competency index, investment ratio, GDP growth, and market share at a 5% significance level. However, company size had a negative and significant effect on ROA at a 5% significance level. Furthermore, liquidity and inflation had a positive effect on the performance of insurance companies, while leverage had a negative effect. However, these effects were not significant at a 5% significance level. Based on these findings, the study suggests that managers of Ethiopian insurance companies should be prepared for economic changes in the country by developing financial plans that consider the impact of changes in GDP. When expanding the company's assets, managers should consider the effect on financial performance. Additionally, managers should focus on maximizing their market by offering new product lines, entering into new market areas, and advertising their services and facilities.

Key Terms: Financial performance, insurance companies in Ethiopia, return on asset, leverage, liquidity, management competency

INTRODUCTION

The financial system is made up of financial markets, financial instruments, and financial institutions. By encouraging saving and investing, connecting savers and investors, and supporting the growth and improvement of financial markets, this system plays a crucial role in the economic development and stability of a nation. The purpose of financial institutions is to ease trade, production, and resource allocation by channeling cash and transferring risks from one economic unit to another. The performance of financial intermediaries, such as insurance companies, can influence the economic growth of a nation by reducing risk and raising significant sums of money, which in turn affects the production of goods and services as well as business profits for companies (Naveed et al. 2011). Indeed, one of the most crucial elements in fostering greater economic growth and financial system stability is the efficiency of financial markets and institutions like insurance firms. Reversely, underperforming financial markets and institutions are a factor in the continued underperformance of the economies of many nations worldwide (Mishkin and Stanley 2009).

According to Augustine & Nwanneka, (2011) the insurance industry is regarded as the backbone of every country's risk management system since it functions as a financial intermediary, ensuring financial security and providing funds for long-term investment. Insurance businesses offer specialized financial services ranging from

risk underwriting to the mobilization of large funds through premiums for long-term investments. The risk-absorption role of insurers fosters financial stability in financial markets and gives economic entities a sense of security. Without insurance, the business world is unsustainable since hazardous businesses may not be able to retain all types of risks in an ever-changing and uncertain industry (Ahmed et al. 2010).

The insurance industry plays a significant role in creating liquidity, lowering transaction costs, facilitating economies of scale in investing, and spreading financial losses. According to Kazeem (2015), the importance of insurance firms for businesses and individuals grows as they reimburse company losses, protecting economic activity in society from collapse. Insurers provide economic and social advantages to society not just by preventing losses but also by reducing worry and fear, increasing employment, and generating accumulated premiums for long-term investment. As a result, insurance firms, like any other company, are expected to continually improve their performance in order to maintain their place in society.

According to Tarawneh (2006), the financial performance of an organization is a measure of how well the firm can use its assets, and it plays a role in raising the market value of that specific organization, which leads to the development of the financial sector and the overall success of the economy. Profitability, according to Malik (2011), is a critical factor in financial performance. A non-profitable firm cannot endure. A very lucrative firm, on the other hand, might provide its owners with a big return on investment. This increased profitability causes firms to improve their financial performance. As a result, the ultimate purpose of a corporate entity is to produce profit in order to ensure the firm's viability under current market circumstances (Mirie and Jane, 2015).

In the insurance industry, performance is typically measured using the following metrics: net premium generated, profit from underwriting operations, return on asset, yearly turnover, returns on investment, and return on equity. According to Walker (2001), insurance performance is classified into two groups. Financial performance is the first category, while non-financial performance is the second. The financial parameters of performance are factors that may be obtained from insurance firms' financial statements, such as profit and loss. Leverage, firm size, premium growth, tangibility, market share, loss ratio or risk underwriting, liquidity, and so forth.

Non-financial features, on the other hand, are factors that cannot be determined through insurance firms' financial statements and profit and loss statements. They include the firm's age, facility location, product and service generation, and scope of operation (Simon-Oke and Olayemi, 2012).

Insurance companies can face various factors that can affect their performance. These factors can be classified as internal and external. Internal factors are within the control of management and include strengths and weaknesses that contribute to differences in profitability between companies. External factors, on the other hand, are outside the control of management and can influence a company's performance. Examples of external factors include changes in the money supply, interest rates, industry growth, inflation rates, industry concentration, and gross domestic product growth. These factors are considered macroeconomic or market-specific factors that management cannot control.

The performance of insurance companies can be assessed by considering various attributes such as firm size, underwriting risk, leverage, age, growth rate of written insurance premiums, and the institutional and political environment. Many studies have been conducted to determine the factors that impact firm performance, including profitability. However, there is limited research on insurance company financial performance in developing countries like Ethiopia. Therefore, this study aims to identify the determinants of financial performance for insurance companies in Ethiopia. The most commonly used measure of profitability and financial performance is return on assets (ROA).

This is therefore, the main objective to conduct this study is to examine and compare the determinant of financial performance in the insurance sector of Ethiopia over the period from 2017 to 2021.

1. LITERATURE REVIEW

2.1. Theoretical and conceptual literature Review

2.1.1. Concept of insurance companies

Scholars from all across the world have sought to define insurance in their own words. According to Kunreuther (2010), insurance is an economic institution that permits the transfer of financial risk from an individual or company to a pooled group of risks through a two-party agreement. For a lesser but guaranteed sum, the insured party acquires a fixed amount of coverage against harm caused by an unpredictable future occurrence. Igbojekwe (2006) described insurance as a contract in which the insured financial institution passes the risk of prospective loss to the insurer, who guarantees to reimburse the former in the event of loss. In exchange for this assurance,

the insured pays an agreed-upon sum known as a premium.

The promisor is known as the insurer, while the promisee is known as the insured. It is frequently represented by an insurance policy, in which the insured receives financial protection from the insurer against damages caused by the occurrence of any future events over which the insured has no control.

Insurance firms are undeniably important because they perform a variety of significant economic and social tasks that are both comparable and unique from those performed by other types of financial organizations. According to Chand (2018), he illuminated the significance of insurance companies for individuals, businesses, and the country's economy. According to his explanation, insurance gives financial help and protection while also reducing business concerns. There is always a risk of unexpected losses, so insurance firms provide coverage for such losses. Insurance businesses produce cash by collecting premiums from a large number of policyholders and investing them in government securities, stocks, bonds, and other investment sectors. These funds are being put to good use for the country's economic growth. Large investments that result in capital formation improve employment chances.

According to Malik (2011), insurance is critical to the growth of commercial and infrastructure firms. Insurance companies enhance financial and social stability, mobilize and channel savings, boost trade, commerce, and entrepreneurial activity, and increase the general welfare of a society. According to Abate (2012), insurance companies help a country's economy in one way by transferring and sharing risk, which can create confidence about the occurrences of uncertain events, and in another way, insurance companies, like other financial institutions, play the role of financial intermediation, channeling financial resources from one to the other.

The insurance industry is organized into several categories, but the two most common are general insurance and life assurance. Life insurers are regarded as financial middlemen, whereas general insurers are risk-takers (Chen and Wong 2004). Motor, fire, accident, oil and gas, contractors' all-risks and engineering risks, marine, credit insurance, bond and surety ship, and so on are all subsets of the general insurance sector. This is a contract between the assurer and the assured in which the assurer agrees to pay benefits to the policyholder if a specific event occurs. Individual life insurance, group life insurance, pensions, health insurance, and annuities are all part of the life assurance sector (Suheyli, 2015).

2.1.2. Financial performance

The achievement of a particular work judged against specified criteria and regarded as the fulfillment of a responsibility is referred to as performance. Performance may also refer to the amount of time and effort put into achieving a specific objective. Goal achievement requires a combination of human, financial, and business resources. According to Nirmal (2004), performance not only denotes the display of something, but it also denotes the quality and efficacy of the results obtained by corporate management. According to Almajali (2012), performance is an outcome achieved by an individual or a group in an organization related to the authority and responsibility given to achieve the goal legally, it is the ability of the firm to gain and manage the company's resources in various ways to develop competitive advantage and achieve the organization's objectives.

Performance assesses how successfully a company can use its resources to create income; in other words, it analyzes total financial performance over a certain time period and may be used to compare the results of similar companies in the same industry. The level of performance of a business over a certain period of time is to be assessed in order to determine the level of the achieved result; analyzing a firm's performance helps decision-makers appraise the outcome of the activities completed. Firm performance can be assessed against the organization's goals and objectives, a benchmark, or the industry average.

According to Chen and Wong (2004), insurance company performance is often measured in terms of net premium-generated profits from underwriting operations, return on assets, yearly turnover, returns on investment, and return on equity. According to Indranarain (2009), these measurements are divided into two categories: profit performance measures and investment performance measures. Profit performance comprises earnings calculated as the difference between revenues and costs. Insurance firms' profit performance is impacted by firm-specific, industry-specific, and macroeconomic variables. There are two types of investment performance. One is the return on assets other than cash used in the firm, and the other is the return on investment operations of the cash surplus produced on operations at various levels.

According to Malik (2011), a firm's financial success may be measured by assessing its profitability. In an ever-changing and competitive globalized world, insurers cannot attract external investors' cash unless they are profitable. Profit enhances insurers' solvency while also motivating policyholders and shareholders to provide

cash to insurance companies (Harrington and Wilson, 1989). Thus, one of the goals of insurance company management is to improve the firm's financial performance in order to achieve profit, which is an underlying condition for running any insurance business.

Financial ratios in financial statements provide distinct indications of financial success. Some of the finest measures of a company's financial success include return on assets (ROA), return on equity (ROE), and earnings per share. ROA is commonly used by financial analysts to assess the financial performance of insurance firms. An increase in the ROA ratio indicates that the comparable business is performing well financially, and vice versa (Epps & Cereola 2008).

2.2. Determinants of Insurance Companies Financial Performance: Empirical Evidences

Many studies on the drivers of the financial success of insurance businesses have been done in industrialized countries. The problem receives minimal attention in emerging Asian, Latin American, and African countries. Few studies on the subject are being undertaken in our nation. To conduct these investigations, it is useful to look at what factors have been addressed in past studies of different individuals from all over the world, including Ethiopia.

Hifza Malik (2011) carried out a study titled "Determinants of insurance company profitability in Pakistan." The researcher's primary goal was to assess the influence of firm-specific factors such as size, age, volume of capital, leverage, and loss ratio on profitability. The researcher obtained secondary panel data from a sample of 35 listed life and non-life insurance firms between 2005 and 2009. Finally, the results demonstrate that the size of the firm and the volume of capital have a major positive and significant association with profitability, whereas the loss ratio and leverage ratio have a significant negative and significant relationship with the profitability of insurance companies. However, the age of the firm has little bearing on its profitability.

Kozak (2011) published a study titled "Determinants of insurance company profitability in Poland." The analysis is based on panel secondary data acquired from 25 Polish insurance firms during a nine-year period from 2002 to 2009. The regression model results show that explanatory variables such as growth in gross written premiums, GDP growth, operating cost reduction, reinsurance utilization, and growth in the market share of companies with foreign ownership have a positive and significant relationship with the performance of insurance companies. Leverage and provision levels have a negative and considerable influence on insurance company profitability. According to the study, the majority of insurance companies in Poland rely on reinsurance and debt to improve their underwriting capacity and stabilize their profitability.

Charumathi B. (2012) did a study on Indian insurance firms titled "Determinants of Profitability of Indian Life Insurers" from 2009 to 2011. The study attempted to model the factors determining the profitability of life insurers operating in India using return on asset as the dependent variable and leverage, size, premium growth, liquidity, underwriting risk, and equity capital as explanatory variables. Finally, the study's findings suggest that the size and liquidity of life insurers have a favorable and considerable impact on their profitability. Leverage, premium growth, and equity capital have all had a negative and severe impact on the profitability of Indian life insurers. The study doesn't uncover any proof that underwriting risk and profitability have a meaningful relationship.

Almajali (2012) investigated the elements that most influence the financial performance of Jordanian insurance companies. The secondary panel data gathered from all insurance companies at the time was evaluated using a variety of basic statistical techniques, such as the T-test and multiple regression. He includes all 25 insurance businesses that were listed on the Amman Stock Exchange between 2002 and 2007. The regression findings revealed that the explanatory variables leverage, size, liquidity, and management competency index have a positive and substantial influence on Jordanian insurance companies' financial performance. Finally, the researcher said that growing the company's assets will result in better financial performance, so managers should think about it. There is also a great demand for highly skilled and competent personnel in the top management team.

Burca and Batrinca (2014) conducted a study titled "Determinants of the Financial Performance of Romanian Insurance Companies." The goal of their research was to identify the elements that influenced the financial performance of Romanian life insurance businesses between 2008 and 2012. The investigation was carried out using particular panel data methodologies. According to the study's regression results, risk retention ratio, company size, and solvency margin have a positive and significant relationship with performance, and financial leverage underwriting, growth of gross written premiums, and risk have a negative and significant relationship with financial performance.

Lee (2014) used panel data from 1999 to 2009 to analyze the link between business-specific characteristics and macroeconomics and profitability in the Taiwanese property-liability insurance sector. The operational ratio and ROA were used to calculate profitability in the research. In both the operational ratio and ROA models, the results reveal that underwriting risk, reinsurance utilization, input cost, return on investment, and financial holding group have a substantial effect on profitability. When compared to other insurance firms, the insurance subsidiaries of the financial holding company have less profitability. Furthermore, the economic growth rate has a large impact on profitability in the operating ratio model but a negligible effect on profitability in the ROA model.

Mirie M. and Jane W. (2015) did a study titled "Determinants of Financial Performance in Kenyan General Insurance Companies." The primary goal of the study was to determine the link between chosen criteria such as premium growth, insurer size, retention ratio, earning assets, investment yield, loss ratio, and expenditure ratio and the financial performance of Kenyan general insurance underwriters. The study used multiple linear regression analysis on three years of data, from 2010 to 2012. The study's findings revealed that financial performance was positively associated with leverage, equity capital, and the management competence index, while it was adversely related to the loss ratio and expenditure ratio. Premium growth, underwriter size, and retention percentage were not substantially associated with financial performance.

Kazeem (2015) studied the influence of firm-specific variables on the financial performance of Nigerian listed insurance businesses from 2006 to 2013 using panel secondary data from twelve listed insurance firms. ROA was used as a proxy for financial performance, and secondary data from the firms' audited financial statements was evaluated using the multiple regression statistical method. Multiple regression results demonstrate that company liquidity, size, loss ratio, and leverage are the most important and significant predictors of financial success in the Nigerian insurance business. As a result, business size, loss ratio, and leverage are all inversely connected. In contrast, the liquidity ratio is considerably and positively associated with financial performance. Finally, the age of the insurance firm and premium increases are not strongly associated.

Boyjoo and Ramesh (2017) looked at the elements affecting the performance of general insurance firms operating in Mauritius during a five-year period between 2011 and 2015. The return on assets (ROA) variable was used in the study to gauge the performance of general insurers. The panel secondary data that was gathered for the study's aim is analyzed using ordinary least squares (OLS) multiple regressions. The study's findings indicate that the following factors have a positive and substantial influence on a company's profitability as assessed by return on assets (ROA): size of the company, leverage, liquidity, underwriting risk, concentration ratio, and investment performance. Re-insurance reliance and growth rate, on the other hand, have an adverse and negligible association with ROA. However, the financial performance of general insurance businesses operating in Mauritius is favorably and insignificantly correlated with net operating expenditure, sales profitability ratio, company age, and premium growth.

3. RESEARCH METHODOLOGY

Data was gathered from all insurance firms in Ethiopia, utilizing a five-year panel dataset (2017–2021) and a quantitative technique for this study. Data from the insurance firms' balance sheets, income statements, and revenue accounts collected from the NBE served as a secondary source of information. The most trustworthy data sources are secondary data sources since these financial statements have previously been verified by independent auditors and approved by the information's consumers. As submitted to them by the Ministry of Finance (MoF), additional macro-level statistics were collected from the NBE (Research Directorate).

The data gathered from data sources was examined using descriptive statistics, Pearson correlations analysis, and multiple linear regression analysis in order to meet the study's goal. Based on data from all insurance companies, mean values and standard deviations, minimum and maximum values, and Pearson correlation matrices are used to analyze the general trends of the dependent and independent variable from 2017 to 2021 and to examine the relationship between the dependent variable and explanatory variables. In order to identify the most important and crucial explanatory factors influencing the financial performance of the insurance business in Ethiopia, ordinary least square (OLS) analysis is also performed using the statistical tool "STATA 11".

4. Data Presentation and Analysis

4.1 Descriptive Statistics

The researcher provides the descriptive statistics for the study's dependent and independent variables in this part. The explanatory variables include leverage, liquidity, inflation rate, managerial competency index, market share, investment ratio, firm size, and GDP growth rate. The dependent variable is the financial performance of the

insurance company, which is assessed by return on assets. 85 observations in all, for the dependent and independent variables, were gathered from 17 insurance firms between 2017 and 2021. The mean, maximum, minimum, and standard deviation of all research variables are included in the study's overall descriptive statistics.

Table 4.1: Summary of descriptive statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
ROA	85	.0827294	.0401972	-.041	.192
LVR	85	.6105039	.1094624	.2554196	.8336244
LQR	85	1.366859	.5180391	.365	3.349
INFR	85	.1017765	.0325062	.075	.168
MCI	85	6.538087	.4856016	4.331781	7.380211
MRS	85	.0598235	.0779609	.001	.374
IVR	85	.1364941	.1019582	.004	.552
GDP _r	85	.093	.0119871	.077	.104
SZC	85	8.660588	.4567206	7.39	9.65

Source: output of STATA

The following narrative includes a summary of each outcome of the descriptive statistics.

In the previous five years, the average ROA for all insurance businesses was 8.3%, with a minimum value of -4.1% and a maximum value of 19.2%. We may infer from the outcome that Ethiopian insurance businesses have, on average, earned 8.3% of their total assets during the past five years. Additionally, the well-run business has a profit before tax to asset ratio of 19.2%, meaning that for every birr invested, there is a return of 192 birr. On the other hand, the insurance firm with the worst financial performance during the previous five years suffered a loss of 4.1% of the entire asset.

Leverage, the study's first explanatory variable, has a minimum value and a maximum value of 0.26 and 0.83, respectively. These data show that, during the study period, there were general insurers with maximum leverage, or a ratio of total liabilities to total assets of 0.83, and general insurers with minimal leverage, or a ratio of total liabilities to total assets of 0.26. However, the ratio of total long-term obligations to total assets is spread out from its mean value of 0.61 by a standard deviation of 0.41. The average leverage value of 0.61 indicates that 61% of the total assets of general insurance businesses were funded by debt, suggesting that debt financing is preferred over equity for these organizations' financing needs.

The liquidity has a mean and standard deviation that are, respectively, 1.37 and 0.52. This suggests that the mean liquidity ratio among insurance businesses is 0.52, with a substantial variance. The liquidity ratio's overall maximum and minimum values are 3.35 and 0.37, respectively. In the previous five years, companies with strong liquidity had liquidity ratios of 3.35, while companies with low liquidity had ratios of 0.37.

One of the macroeconomic factors included in this analysis was the average annual inflation rate, which was 10.2% for the previous five years. The year 2018 saw the highest inflation rate ever recorded at 16.8%, whereas the year 2015 saw the lowest inflation at roughly 7.5%. Over the studied periods, the inflation rate was distributed toward its mean with a standard deviation of 3.25%. This suggests that Ethiopia's inflation rate throughout the research period was not very stable, which may have had a minimal impact on the financial health of the insurance industry.

The management competency index for insurers throughout the chosen period has a mean value of 6.54 and a standard deviation of 0.486. The management competency index has a maximum and a minimum value of 4.33 and 7.35, respectively. According to this, the manager who performs the best makes a profit of 22,387,211 Birr, while the manager who performs the worst generates a profit of 21,3798 Birr.

The sole industry-specific element examined in this study to determine its impact on the financial performance of an insurance firm is market share. It is calculated using the ratio of business gross premium to overall industry gross premium. Market share ranged from 0.1% for the worst-performing firm throughout the research period to 37.4% for the company with the best performance. This demonstrates a very broad range of variation in the market share of insurance companies. Some insurance companies are new to the market, and this huge range of variation may have an impact on how well they operate in Ethiopia. The market share of each insurance company has a standard deviation of 0.78, meaning that the market share of insurance firms in Ethiopia deviates from the mean over time by the specified amount across insurance businesses.

GDP growth is one of the macroeconomic variables considered in this analysis; throughout the last five years, the country's economy has had an average real GDP growth rate of 9.3%. Between the years of 2017 and 2021, the economy grew at its highest and lowest rates, 7.7% and 10.4%, respectively. There is no difference in GDP value across insurance firms; it is the same across all of them.

Investment ratio, a firm-specific statistic utilized in this study, is calculated by dividing investment by total assets. The mean and standard deviation of its investment ratio are 14% and 10%, respectively. This suggests that there is a 10% moderate variability in the liquidity ratio across insurance businesses with mean values. The entire maximum and lowest numbers for investment ratios are, respectively, 0.4 percent and 55 percent. In the last five years, highly invested companies have had investment ratios of 55%, whereas newer companies with lower investment involvement have had investment ratios of 0.4%.

Investment ratio, a firm-specific statistic utilized in this study, is a research variable that also reveals significant fluctuation over the previous five years across insurance companies in Ethiopia. Therefore, as indicated by our regression result, the significantly deviating size may have a major influence on the financial performance of insurance enterprises in Ethiopia.

4.2. Correlation Analysis

Table 4.2 Correlation Matrix Table

	ROA	LVR	LQR	INFR	MCI	MRS	IVR	GDPr	SZC
ROA	1.0000								
LVR	0.0946 0.3891	1.0000							
LQR	0.0142 0.8972	0.3046* 0.0046	1.0000						
INFR	0.0075 0.9454	0.0080 0.9421	0.1070 0.3296	1.0000					
MCI	0.6098* 0.0000	0.0289 0.7931	0.0230 0.8343	0.1204 0.2723	1.0000				
MRS	0.5657* 0.0000	0.0320 0.7713	-0.1090 0.3208	0.0337 0.7596	0.5206* 0.0000	1.0000			
IVR	0.1753* 0.0885	0.0037 0.9732	0.0166 0.8805	0.0272 0.8050	0.0267 0.8081	-0.0402 0.7150	1.0000		
GDPr	0.1883* 0.0844	0.1036 0.3453	-0.0273 0.8042	-0.4587* 0.0000	-0.1570 0.1513	-0.0282 0.7980	-0.0051 0.9630	1.0000	
SZC	0.3629* 0.0006	0.0372 0.7353	-0.0656 0.5510	0.2430* 0.0250	0.7842* 0.0000	0.5747* 0.0000	-0.0012 0.9910	-0.3271* 0.0022	1.0000

Source: output of STATA

The relationship between the independent variables leverage, liquidity, management competency index, investment ratio, company size, market share inflation, and GDP and the dependent variable return on assets (ROA) demonstrates that, at 0.1 levels of significance, the explanatory variables management competency, market share, company size, leverage, GDP, and investment ratio are significant and positively correlated with ROA. Inflation and liquidity do not significantly affect ROA. The correlation matrix's findings indicate that the managerial competency index and market share, calculated as the ratio of premium to total gross premium for the sector, have the highest positive percentages.

The managerial competency index and financial performance of insurance organizations have a 0.61 connection coefficient. This suggests that the managerial competency index has a 61% positive correlation with financial performance. As a consequence, the data showed that the management competency index and return on assets are

directly related.

Market share analysis reveals a correlation value of 0.57, significant at the 1% level. The indicator has a considerable and positive correlation with the Ethiopian insurance industry's financial performance. This suggests that the market share of the insurance firm will expand along with its financial success and that the relationship will be substantial at a 1% level.

ROA and firm size have a positive link with a correlation value of 0.36, which is significant at the 5% level of significance. The correlation coefficients between ROA and the explanatory variables GDP, investment ratio, inflation, leverage, and liquidity are 0.21, 0.19, 0.18, 0.09, and 0.01, respectively. However, the link between ROA, liquidity, and inflation is negligible at the 10% level of significance. The correlation coefficient between GDP and investment ratio is strong at the 10% level of significance. The correlation matrix's final conclusion reveals that ROA and liquidity have the lowest correlation among the independent and dependent variables.

4.3. Regression Analysis

To determine the strength and direction of each explanatory variable's influence on the dependent variable, the researcher used OLS multiple regressions. The dependent variable in this regression study is ROA, while the independent variables are the ratios of leverage, liquidity, inflation, management competence index, market share, and investment, as well as the size of capital and GDP growth rate. The following regression equation was calculated:

$$ROA_{it} = \beta_0 + \beta_1 Lvr_{it} + \beta_2 Lqr_{it} + \beta_3 Infr_{it} + \beta_4 Mci_{it} + \beta_5 Mrs_{it} + \beta_6 Ivr_{it} + \beta_7 GDP_{it} + \beta_8 Szc_{it} + \varepsilon_{it}$$

β_0 = Constant

$\beta_1, \beta_2, \beta_3, \beta_4, \beta_5, \beta_6, \beta_7$ and β_8 = Coefficients of independent variables I = Insurance company and $i = 1, 2, 3, \dots, 17$

t = The index of time periods and $t = 1, 2, 3, 5$

$\varepsilon_{it} = a_i + u_{it}$ when a_i all unobserved, time constant factor that affect ROA it

u_{it} is often called the idiosyncratic error or time-varying error

Table 4.3 Result of regression

. reg ROA LVR LQR INFR MCI MRS IVR GDP_r SZC

Source	SS	df	MS	Number of obs = 85	
Model	.083165771	8	.010395721	F(8, 76) = 15.03	
Residual	.052563006	76	.000691619	Prob > F = 0.0000	
Total	.135728777	84	.001615819	R-squared = 0.6127	
				Adj R-squared = 0.5720	
				Root MSE = .0263	

ROA	Coef.	Std. Err.	t	P> t	[95% Conf.	Interval]
LVR	.0002728	.0004006	0.68	0.498	-.000525	.0010706
LQR	-.0003875	.0059866	-0.06	0.949	-.0123109	.0115358
INFR	.1264848	.100992	1.25	0.214	-.0746582	.3276278
MCI	.0592433	.0098717	6.00	0.000	.0395822	.0789044
MRS	.2216068	.0465396	4.76	0.000	.1289152	.3142984
IVR	.0675112	.0282256	2.39	0.019	.0112951	.1237273
GDP _r	.7532727	.2871384	2.62	0.011	.181387	1.325158
SZC	-.0350952	.0117249	-2.99	0.004	-.0584474	-.011743
_cons	-.1059258	.0853078	-1.24	0.218	-.2758311	.0639794

Source: output of STATA

The next section of the findings discussion focuses on the results of the multiple regressions and the impact of each explanatory variable on the financial performance of insurance businesses in Ethiopia.

Leverage

The debt-to-equity ratio is a measure of leverage that takes into account the capital structure of the company and the assessment of the relative risk and return associated with long-term debt and equity. The coefficient of leverage ratio is positive (0.0002728) and statistically insignificant with a p-value of 0.498, which is higher than 0.05, indicating that using the standardized coefficient and holding all other factors constant, a 1% increase in the leverage of insurance firms in Ethiopia would not have any significant impact on the industry.

Liquidity

The current asset-to-current obligation ratio is a measure of liquidity. Current assets divided by current liabilities yields a liquidity coefficient with a P-value of 0.949 and a value of -0.0003875. The liquidity and return on assets (ROA) of Ethiopian insurance businesses have a negligible connection. Since ROA and liquidity have a weak connection (9%), the outcome is contradictory to the study's premise but compatible with the correlation analysis's findings. The null hypothesis, according to which there is a strong negative association between liquidity and ROA, is thus rejected by the researcher.

A 1% increase in the liquidity of insurance companies in Ethiopia causes, on average, a 0.04% decline in their financial performance when using a standardized coefficient and keeping all other variables constant. However, as can be seen, the performance decline was small and inconsequential. This indicates that there is insufficient data to back up the claim that liquidity and ROA have a negative connection. Despite being minor, the impact of increased insurance company liquidity on financial performance is shown to be negative by the coefficient. The outcome is consistent with earlier research, including Hadush (2015), Hana (2012), Mirie and Jane (2015), and Nikhel B. et al. (2015), which demonstrated a positive association between liquidity and ROA.

Inflation

The financial health of insurance firms may be impacted by inflation, which might have an impact on both their obligations and assets. In anticipation of inflation, claim payments rise along with the reserves needed to cover the increasing claims, which has the unintended consequence of lowering technical results and profitability. The impact of inflation on the financial performance of Ethiopian insurers was insignificant since the inflation coefficient, 0.1264848, was positive but not statistically significant ($p = 0.214$). This suggests that, when all other variables are held constant and the standardized coefficient is used, a 1% increase in inflation for insurance businesses in Ethiopia will, on average, result in a 12% improvement in their financial performance. However, the conclusion is not statistically significant at the 5% level of significance. Since the study was unable to gather enough statistical evidence to demonstrate a substantial and negative link between inflation and ROA, one may infer from the actual results that inflation has no bearing on the financial performance of Ethiopian insurance businesses. The findings of Tariku (2017), Andres C. (2017), Godfrey (2012), and Hadush G. (2015), who discovered a negligible positive association between inflation and ROA, are likewise compatible with this outcome.

Managerial competency index

The log of the ratio of profit to the total number of the top management team, which measures managerial skill, is statistically significant at the 1% and 5% significant levels with ROA. Consequently, management skills have a significant impact on enhancing the financial performance of insurance firms in Ethiopia. 0.0592433 is the regression coefficient, while 0.000 is the p-value. As a consequence, the findings support the study's premise and correlation analysis. According to the management competency index's standardized coefficient, when all other variables are held constant, an increase in the management competency index of 100 results in a 6% increase in return on assets. The outcome recommended that insurance businesses should concentrate on the management team's competence. The performance of the organization improves as the management team's competencies grow. This may be as a result of the professional's assistance to the insurance firm in managing risks, discovering and developing investment opportunities, as well as making optimal use of resources and managing working capital. The outcome is consistent with Almajali (2012) and Wangugu (2012)'s conclusions, which state that the managerial competency index has a significant impact on profitability.

Market Share

An industry-specific metric for determining market share is the ratio of an insurer's total gross premium to the total gross premium of the sector. The market share coefficient is positive (0.2216068) and statistically significant (p-value 0.000), which is less than 5% and significant even at the 1% level. As a consequence, the findings support the study's premise and correlation analysis. The positive correlation between market and ROA demonstrates that market share and the financial success of Ethiopian insurance businesses, as measured by ROA, are directly related. When all other variables are held constant, an increase in market share of 1% results in a 23% rise in the financial performance of the insurance firm, according to the standardized coefficient of management competency index. This is because a larger market share offers insurance firms the opportunity to use economies of scale to lower costs and increase their ability to set prices. This positive link was anticipated, and the outcome is consistent with earlier research by Tariku (2017), Gale (1972), and Chen-Ying Lee (2014), which discovered a positive correlation between market share and ROA.

Investment ratio

The ratio of investments to total assets is used to calculate the investment ratio. The investment ratio coefficient is 0.675112, and it is statistically significant at the 5% level of significance with a p-value of 0.025, which is less than 0.05. As a consequence, the findings support the study's premise and correlation analysis. According to the standardized coefficient of investment ratio, an increase in investment ratio of 1% results in an increase in return on assets of 7% when all other variables are held constant. This indicates that insurance firms should expect to perform financially better if they devote more of their available resources to profitable ventures.

The research's findings are consistent with those of other studies, including those by Burca and Batrinca (2014), Shiu (2004), Lee (2014), and Boyjoo and Ramesh (2017), which were carried out in different nations and discovered a positive and substantial association between ROA and financial success.

Gross Domestic Product

The most significant macroeconomic metric of economic development is GDP. The increase in the nation's gross domestic product serves as a proxy for GDP. GDP has a positive coefficient of 0.7532727 and is statistically significant at the 5% level of significance with a p-value of 0.011, which is less than 0.05. As a consequence, the

findings support the study's premise and correlation analysis. When all other variables are held constant, the standardized coefficient of gross domestic product demonstrates that an increase in domestic product of 1% results in an increase in the financial performance of an insurance firm of 75%. Economic growth can help insurance companies perform better by increasing demand for financial services, which in turn increases insurers' cash flows and profit margins. This is indicated by the significant positive coefficient of the variable, which shows how closely the two are related. The need for insurance services would undoubtedly rise as the economy grows rich, which might ultimately lead to significant returns or profit margins for the insurers. This study's findings are consistent with those of Tariku (2008), Murungi (2014), Doreen (2013), and Lee (2014).

Company Size

The insurance firm's entire assets are used to calculate its business size. With a regression coefficient of -0.0350952 and a p-value of 0.005, the study's regression results showed a significant and adverse link between firm size and the financial performance of insurance companies in Ethiopia. As a consequence, the findings support the study's premise and correlation analysis. According to the standardized coefficient of size, an increase in size of 100 results in a 3.5 drop in the average return on assets, with all other variables being held constant. As a result, larger insurance companies may not be more effective than smaller ones since they lack a competitive advantage.

Our a priori anticipation is at odds with the negative company-size impact. This suggests that the ROA decreases by an average of 3.5% for every unit increase in company size. This can be a result of the scale disadvantages insurance companies have experienced as a result of unchecked size growth. According to Majumdar (1997), when businesses get larger, they may have inefficiencies that worsen their financial performance. The results are in direct opposition to the resource-based hypothesis, which asserts a large and positive association between business size and financial success.

This study's regression results are consistent with those of Lee (2014), Cummins and Nini (2002), Kazeem (2015), Derbali (2014), and Mwangi and Murigu (2015), who discovered a negative relationship between firm size and the performance and profitability of insurance companies.

5. Summary, Conclusion and recommendation

5.1. Summary and findings

The following is a significant summary of the study findings based on analysis:

- The leverage ratio coefficient is positive (0.0002728) and statistically insignificant with a p-value greater than 0.05.
- The liquidity coefficient, as measured by current assets to current liabilities, is -0.0003875, with a P-value of 0.949, implying an insignificant negative link between liquidity and the return on assets (ROA) of Ethiopian insurance businesses.
- The inflation coefficient was positive (0.1264848), but it was not statistically significant (p-values = 0.214), indicating that the influence of inflation on Ethiopian insurers' financial performance is negligible.
- The management competency index regression coefficient is 0.0592433 with a p-value of 0.000, which is significant at the 1% and 5% levels of significance.
- The coefficient of market share is positive (0.2216068) and statistically significant with a p-value of 0.000, which is less than 5% and also significant at the 1% level.
- The investment ratio coefficient is 0.675112 and statistically significant at the 5% significance level with a p-value of 0.025, which is less than 0.05.
- The GDP coefficient is positive (0.7532727) and statistically significant at the 5% significance level with a p-value less than 0.05.
- With a regression coefficient of -0.0350952 and a p-value of 0.005, the study's regression results demonstrated a significant and negative association between firm size and the financial performance of insurance companies in Ethiopia.

5.2. Conclusion

To explain the factors affecting insurance company financial performance, descriptive statistics, Pearson correlation matrices, and random effect regression analysis were used. The study found that the factors chosen explained 61.3% of the variation in ROA of insurance businesses in Ethiopia. This suggests that the independent variables leverage, liquidity, inflation rate, managerial competency index, market share investment ratio, firm

size, and GDP growth rate explain approximately 61.3 percent of the variation in insurance companies' financial performance.

At the 5% level of significance, the regression coefficient of firm size is a negative and statistically significant indicator of financial performance. This indicates that larger insurance companies may be inefficient, and their scale does not provide them with a competitive edge in terms of increasing their performance. This might be attributed to corporations purchasing machinery, expanding their branches, and implementing new technologies, all of which raise their overall assets in order to enhance their profit by underwriting more policies. However, due to ineffective management and other circumstances, they are unable to achieve the anticipated objectives. As a result, a growth in assets affects the financial performance of an insurance firm, as measured by ROA.

The regression and correlation analyses indicate a positive and substantial association between the managerial competency index and insurance company financial performance. This indicates that insurance businesses with more professional management are projected to be more lucrative. This is because skilled managers help the insurance firm make better and more efficient use of corporate resources through investment research, analyzing and managing product mix, solid market analysis, risk management, improved understanding of future risks, and appropriate response. As a result, we may infer that skilled management is critical for the success of insurance firms.

According to the regression and correlation analyses, there is a positive and substantial association between the managerial competency index and insurance company financial performance. This means that insurance businesses with more skilled management are projected to be more lucrative. This is because skilled managers help the insurance firm make better and more efficient use of its resources, conduct investment research, review and manage the product mix, conduct excellent market analysis and risk management, better analyze potential risks, and take necessary action. As a result, we may infer that skilled management is essential for the success of insurance firms.

The study's regression and correlation analysis results demonstrate a favorable and highly significant association between insurance businesses' financial performance and the real GDP growth rate. This finding means that as a country's GDP rises, so will its investment. As a consequence, the chance of selling insurance policies and investment possibilities to insurance firms rises, and insurers are likely to gain in the form of larger profits. As a result, GDP is the most important component whose rise or decline has a significant impact on the performance of insurance companies.

The leverage ratio coefficient is positive (0.0002728) and statistically insignificant with a p-value greater than 0.05. A positive and negligible relationship between the loan-to equity ratio and financial performance means that insurance businesses in Ethiopia from 2014 to 2018 were not significantly influenced by increasing or reducing the leverage ratio. Thus, it can be stated that whether insurance businesses utilize debt financing or equity financing to raise total assets or to invest, it has no influence on their financial performance.

According to the regression results, there is no significant association between inflation and insurance company performance at the 5% level of significance over the research period. This might be because there has been no major change in the country's inflation from 2017 to 2021, and also because insurance firms include inflation when giving policies to clients, and clients receive a fixed predefined amount when they experience a loss. As a result, changes in the inflation rate have no influence on the performance of Ethiopian insurance businesses.

At the 5% significance level, the investment ratio coefficient is a positive and statistically highly significant driver of financial performance. It reflects the fact that higher investment returns result in improved financial performance for insurance businesses. This is because an increase in investment income will allow you to meet unforeseen losses and remain competent in the financial business. As a consequence, policyholders' trust grows, and they gain an edge in attracting more policyholders, leading to stronger financial performance. Thus, the investment ratio is the most important driver of insurance company success in Ethiopia.

5.3. Recommendations

The researcher has made the following suggestions based on the study's findings.

- The study's findings indicated that insurance businesses' financial success was strongly and favorably impacted by their market share. Managers must expand the firm's market share in order to improve the company's financial performance. This might be accomplished by creating additional branches in other sections of the country, introducing new product lines, and publicizing the company's services and facilities.

- Companies should prepare for changes in GDP growth, even if macroeconomic conditions are outside the management's control. This may be accomplished by creating financial plans such as a cash budget, pro-forma balance sheet, and income statement, which will allow insurance businesses to readily adapt to the country's economic developments.
- Insurance company managers should undertake a cost-benefit analysis prior to increasing their assets, and each expansion in assets requires strong supervisory follow-up and management because increasing an asset has a negative influence on the performance of insurance firms.
- Managers of insurance businesses should analyze various investment choices and engage in investments to improve the firm's performance.
- Firms should improve management competency among their employees through training and other means, as it is favorably connected to financial success. Insurance businesses must also retain competent and experienced managers by paying them more and providing other advantages.
- Management bodies of insurance businesses should try to emphasize these variables by studying their impact while making financial choices, establishing financial plans and budgets, and so on.
- Finally, due to time and data constraints, this study focused on various firm-specific, industry-specific, and macroeconomic financial performance drivers of insurance businesses in Ethiopia. As a result, future research may focus on expanding time frames and examining variables such as branch number, average claim per revenue, revenue per policyholder, average cost per claim, and investment mix to determine which variables are powerful determinants of financial performance.

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