PORTFOLIO MANAGEMENT AND PROFITABILITY OF UNIT TRUST COMPANIES IN KENYA

BY

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D53/CTY/PT/23228/2011

A RESEARCH PROJECT SUBMITTED TO THE SCHOOL OF BUSINESS IN PARTIAL FULFILMENT FOR THE AWARD OF DEGREE IN MASTER OF BUSINESS ADMINISTRATION (FINANCE) OF KENYATTA UNIVERSITY

April, 2022

DECLARATION

This project is my original work and has not been presented for a degree in any other university or any other award.

Sign…… Date…….

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This research project has been submitted for examination with my approval as the university supervisor.

Sign …… Date...……

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DEDICATION

I dedicate this project to my husband Nduma and my sons Jamal, Jude and Jesse.

ACKNOWLEDGEMENT

I want to thank my project supervisor Mr. James Muturi of Kenyatta University. Mr. Muturi has always been a help in my project. He guided and directed me on how to do this project. I thank my parents and family who were always supportive during my years of study and when I'm doing this project and I wouldn't be able to complete this project without their support. I thank God too. This study would not have been possible without his mercy and love.

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ABBREVIATIONS AND ACRONYMS

CMA	Capital Markets Authority
EUT	Expected Utility Theory
JSE	Johannesburg Stock Exchange
LUSE	Lusaka Stock exchange
MANCO	Management Company
MFI	Micro Finance Institutions
MPT	Modern Portfolio Theory
NSE	Nairobi Securities Exchange
P/B	Price to Book
P/E	Price to Earnings
ROA	Return on Assets
ROE	Return on Equity
SPSS	Statistical Package for Social Science
UT	Unit Trusts

OPERATIONAL DEFINITION OF TERMS

Expected return **:** earnings, which investors forecast in an investment with known or predicted return rate.

Liquidity **:** how fast a financial security can be traded at its current market price.

Portfolio management: it is assessing options on what to invest, tallying investments to goals, asset earmarking for people and companies, and weighing risk contra to performance.

Profitability **:** capacity of businesses to make positive earnings given its current resources relative to other investments.

Return on assets : profitability ratio measuring corporate gains given the resources that a company has applied.

Return on equity : measure of financial profitability obtained by dividing net income by shareholders' equity.

Risk : variability of returns on asset.

Standard deviation : measure of dispersion from the mean acquired by calculating square root of the variance.

ABSTRACT

The choice of portfolio and the ideal allotment of funds under various options for investment is a subject of interest in economics. Investment is guided by three basic needs: income, capital preservation and capital appreciation. A unit trust company is a financial service organization that gets money from shareholders, invests it, earns returns, tries to increase its value and agrees to pay shareholders cash when they need it and the current value of investment. Unit trusts advantages include diversification, high liquidity, and professional management. In Kenya unit trusts companies contribute immensely to the countries' gross domestic product and currently the sector has mobilized funds amounting to billions of Kenya shillings. Portfolio management are of great importance when it comes to profitability of unit trusts companies. In Africa, unit trust companies are used for investing. Unit trusts are designed to enable even individual and institutional investors to invest. However, unit trust companies have profitability challenges and portfolio management affects profitability of unit trust companies in Kenya. This study focuses to probe effects of portfolio management and profitability of unit trust companies in Kenya. Specific objectives of this study are:, to establish the effect of expected rate of return on profitability of unit trust companies in Kenya, to establish the effect of risk on profitability of unit trust companies in Kenya and to establish the effect of liquidity on the profitability of unit trust companies in Kenya. Theories assessed are Modern Portfolio Theory, Expected Utility Theory, Capital Asset Pricing Model and Financial Intermediation Theory. The research design applied is descriptive research design. Target populations are portfolio managers in the 24 unit trust companies and a census study was adopted as sampling procedure. The researcher used structured questionnaires to collect data. Pilot testing was done to determine validity of research instrument. Content analysis was conducted to analyze the respondents' views concerning portfolio management and profitability of unit trust companies in Kenya. Fieldwork was done later. Completed questionnaires were checked to ensure completeness and consistency. Content analysis and descriptive analysis was conducted. Data was analyzed using mean score, mean weighted averages, percentages, standard deviations, and regression analysis. Tables and other graphical presentations were used for data collected exhibition for easier understanding and analysis. The study found out that expected rate of returns has a positive and significant effect on profitability of unit trust companies. Risk has a positive and significant effect on profitability of unit trust companies. Liquidity has a positive and significant effect on profitability of unit trust companies in Kenya. The study established Portfolio management has a positive and significant effect on profitability of unit trust companies in Kenya. The study recommends Units trusts in the country to adopt portfolio management, expected rate of returns, risk and liquidity to be considered in making investment decision to increase the profitability. The study will provide insight to the investors by providing a more modern approach in evaluating unit trusts profitability and help portfolio managers hold profit generating portfolio for their company and investors. The findings will also benefit regulators to come with new policies and regulations to favor growth and profitability in the unit trust industry and finally aid researchers to form basis for their studies.

CHAPTER ONE

INTRODUCTION

1.1: Background of the Study

Portfolio management ascertains strengths, weaknesses, opportunities and threats in the way out between debt vs. equity, domestic vs. international and growth vs. safety in setting out to boost returns under acceptable level of risk (Singer & Greg Fedorinchik, 2009). Unit trusts has various advantages like diversification, high liquidity and professional management. Unit trusts capitalize on immense purchases and lessen settlement costs for investors. Major Unit Trust companies are precious to investors because of economies of scale and benefits attained because of split research funds and data, less marketing and allotment prices (Pathak, 2014).

Individual investors or retail investors are the ones who invest directly for themselves. Institutional investors are entities like investment companies, commercial banks, insurance companies, pension funds and other financial institutions. The main reason investors choose to be institutional investors is because institutional investors can achieve economies of scale, demographic pressure on social security and the changing role of banks (Konar,2019).

Investors can use direct or indirect investing. Key difference between the two is that in direct investing, investors trade and manage their securities on their own while indirect investing entails using a financial intermediary to invest. In direct investing investors assume all the risks and the profits gained is determined by the direct investor efficiency in selecting the portfolio well. The main advantage of indirect investing is its ability to use professionals like UT companies and brokers to invest therefore the investor can focus on other things. Both direct and indirect investors

get dividends, interests and capital gains and also pay for charges like management fees (Konar,2019).

Institutional investor usually has more advantage than the individual investor when it comes to information. This is because institutional investor benefits from large scale and professional knowledge therefore making information collection and information analysis easier and more accessible to them. Furthermore, institutional investors share information with other shareholders and stakeholders and the information may influence the market. Institutional investors are usually the largest shareholders hence they play a major role in corporate governance (Shen & Cao, 2011).

Jonava (2009), argues that evaluating portfolio results start by reviewing all assets under management and movement of cash resulting to fund's gains. Big companies, which connects market products to contribution margin to attain portfolio excellence can be elusive. In order to balance profits and ensure efficiency in assets usage in a company, an efficient portfolio management system is needed at each business unit. Higher returns require portfolio managers to lay out and utilize strategies well.

Choosing a portfolio and allocating resources under various investment options is a familiar topic. Gruber (2012) remarked that based on rate of return, UT holders make a choice between real and financial investments. Tornell (2010) reveals given uncertainty in third world countries, real sector companies prefer investing in higher reversible liquid assets in the financial industry which are more profitable than non-current assets.

Jonava Inc (2009) argues that performance measurement starts by evaluating the portfolio valuation reports and cash transactions in order to establish a return rate. In big corporations, linking products to higher profit margin to attain higher returns may not be easy. Balancing

profitability and efficient utilization of resources in a company need a well- established portfolio management in the company to ensure higher returns.

Investors expect higher returns for their investments. Roll & Ross (2012) using Arbitrage pricing theory shows the relationship between portfolio returns and single asset return via linear collaboration of various independent macro-economic variables. Investment return measures increase in wealth from a particular venture which is in percentage form. Murumba (2012) reveals that expected return is a main component and has an unswerving connection as ultimate gauge of an investment. Higher expected returns make investors invest in a particular security. The higher the number of investors the more likely the company is to make profits because increase in returns persuades investors to undertake an investment.

The effects of uncertainty, risk and volatility of unit trust companies in third world countries has sparked a great interest in researchers especially under the decreasing fixed capital formation rates in first world countries in 2000s (UNCTAD, 2003). The empirical literature is not wide in regard to studies that look into risk and uncertainty in investment. Portfolio management, risk and liquidity is not an area that has been studied greatly by researchers.

In a risk study analysis by Murumba (2012), the study reveals that in making investment decisions, investment managers of investment companies, risk was one of the major factors that influences decision making. This therefore means that how risky or less risky securities are will determine the decision of investment managers. However, it does not translate to the riskier the investment, the higher or the more the returns it can generate. Risk affects profitability of unit trusts companies because when choosing fund portfolio, risk influences decision-making of investors on whether to invest or not to invest, the higher the number of investors the higher the profitability of unit trust companies due to economy of scale.

The conducted analysis of the recent research publications on the case of short-term private investment has shown that the short-term private investors require high liquidity and low risk instrument and can tolerate comparatively low returns, and that the best tools for such investments are money market instruments (Konar, 2019). Investment companies use resources to do detailed economic analysis and analyze industry trends. The financial trends are taken into consideration as the budgets are formulated. Michuku (2012) reveals there are needs among investors for real investment trusts so as to provide liquid investments which construct a well-diversified investment portfolio. His study also revealed liquidity affected positively the profitability of the unit trusts in Kenya.

In Kenya, unit trusts began after ratification of CMA sanctioned in Section 30 of CMA Act which ratify companies in boosting UT under Capital Markets Regulations, 2001. Total funds managed increased by 21.2 per cent to Ksh38.1 billion in 2014 from Ksh17.6 billion in 2010. The reason is because stock quotes increased, costly bond quotations in addition to increased number of participants in UT. Back in 2012, NSE 20 share index increased with 28.95 percent and NASI increased with 39.42 percent. Aggregate UT profits increased up to KES4.8 billion as compared to KES931.1 million in the previous year (East African, 2015).

As at 30th June 2012, total UT funds were 951 and the number of UT companies were 42 in Africa. A research by Zamara showed South Africa held R3.3 trillion in UT while during the same period in 2011 they only held R3.1trillion in UT showing 6% increase. A report by world bank in June 2013 totals Africa's asset management increased by 4.4% in 2012. The report showed that South Africa UT growth will increase by 4.9% in 2013, 5.2% in 2014 and 5.4% in 2015 KPMG (2013).

Unit trusts funds around the world rose from 69,492 in 2010 up to 79,669 in 2018. Globally funds under management in UT rose from four trillion United States dollars in1993 to thirty three trillion

United States dollars in September 2018, meaning rise in of UT funds in USA, European countries, Asian countries and other parts globally (ICI, 2018). United States share of unit trusts is still the biggest globally having funds under management of $17.87 trillion as at December 2017. This is fifty percent of the $33.4 trillion funds under management in the whole world. Net assets also grew by $818 billion in 2013 attributed to increase in equity fund. New capital injection in the four UT funds was $102 billion in the year 2014 (Wells Fargo, 2017).

1.1.1. Portfolio Management

Portfolio management is selection of the right investment policy for clients while creating a balance between lowest risk and highest return. Portfolio management involves managing investments which can be bonds, stock shares, cash etc. so as to maximize returns within a certain time period. Portfolio managers are the ones who manage the client's funds. Portfolio Managers can manage the funds actively or passively (Singer & Greg Fedorinchik, 2009).

Flourie et al (2001) outlines that UT has three constituents: Fund, Trustee and Management Company (MANCO). MANCO is divided further into fund management, fund administration and marketing (Flourie et al, 2001). Flourie et al (2001) reveals a UT fund should invest as stated in the investment mandate agreed between MANCO and trustee. Investment mandate is an individual official paper because of its complexity in setting out the objectives and guidelines of UT (Bernstein, 1995). The investment mandate doesn't have legal standing, it is there to categorize the different UT fund. Yakov (1999) showed by MANCO and portfolio manager to signing the investment mandate, this warrants zero wrangles in viewpoints.

Globally, according to Neghondw (2005), in 1959 Malaysia was the first to establish UT in Asia. The company was called Malayan Unit Trust Ltd. UT industry in Malaysia has existed for four

decades (Neghondw, 2005). In the beginning, the UT industry in Malaysia had a slow growth in terms of the profit levels and new investments because the public wasn't investing greatly Jorion (2000), the first twenty years had only five new UT companies and a total of eighteen funds.

Regionally, according to Muringari (2004), the bad macro-economic environment from 2000 to 2004 delayed the success of UT. Inflation in Zimbabwe during 2000 to 2004 lessened the savings of individuals and hence the investment capability of individual investors. Decrease in savings was a setback indirectly to the success and profitability of UT companies (ZAUT, 2004). Muringari (2004) in his analysis revealed that a reduction in savings is a contributor in the decline of unit trust profitability in 2004.

UT managers in Kenya place their money mainly in banks or stock market in order to avoid risk. This limits profits and growth of UT companies' CMA (2010). The average growth of UT has been Sh1.9 per year to Sh17.6 billion during the last nine years, this is slower than pension funds which doubled from Sh176 billion in 2005 to Sh 420 billion. Total UT assets increased by 68 per cent in 2010 because of rise in individual stock prices an increase in government bonds purchase (Mugwe, 2011). Total assets managed by UT companies rose from Sh11 billion to Sh28 billion in 2010 from Sh16.8 billion in 2009 CMA (2011). Profit multiplied almost four times to Sh3.8 billion in comparison to 2009 at Sh868 million. The UT industry announced profits after tax of Sh3.3 billion from Sh446 million with British American Asset Managers (BAAM) being the market leader in the industry based on assets under management.

Fama (2001) has studied the unit trust manager's ability of selecting the stocks from the market and their market timing. He has suggested that the overall performance of the managed portfolio be depended upon certain parameters and the performance can be broken down into several

components like those that one of them is the market timing in the market price movements. These studies emphasized on the market timing expertise of the portfolio managers in choosing the securities. Fama (2001) has argued that the returns of the fund are not only fully dependent on the fund manager's ability of selecting the best securities at a particular risk level but also part of the returns also arise due to the prediction of selecting the securities with the correct market timing.

In active portfolio management, the portfolio managers often buy and sell securities to maximize funds returns. When actively managing fund's portfolio managers aim to outperform the set benchmark so as to add value to the portfolio. When it comes to risk and performance measures, benchmarks are important in order to gain clear measurements in accordance with the investment strategy. Measuring actively managed funds relies on historical returns and benchmark index. Tracking error evaluates standard deviation of variance between expected return and index's return (Johan, 2013).

Fox and Krige (2013) probed sources of performance in South African local stocks in order to rule which segment of portfolio's profits is gained by active sector allocation as compared to equity selection. Sharpe's (1992) usage of asset-class factor model was acclimatized as epitome for allocating asset. Fox and Krige (2013) established blooming shares samples, UT outperform through sector allocation, though redressed by bad selection of asset.

Passive portfolio management involves matching a portfolio with the current market scenario. It doesn't involve any forecasting. It aims on minimizing investment fees and avoiding mistakes of failure to correctly predict the future. Passive portfolio management imitates performance of an index. It involves buying one or more index funds. The portfolio under management tracks an index in order to achieve low turnover, low management fees and diversification. Alpha is used

to measure portfolio's return vis a vis benchmark while adjusting for risk. The most widely used benchmark is the S&P 500. An alpha greater than zero depicts more return for the given amount of risk. Alpha less than zero indicates the security has underperformed the benchmark; the return is too little for the risk assumed. Investors prefer higher alphas (Johan, 2013).

South Africa unit trusts are categorized as per the assets forming fund portfolio and risk/reward outlook. The advantage of this is that UT companies are able to keep up their distinctive of their funds and subdue competition (Joubert, 2002). According to Lambrechts (2017), Portfolio specialization caused UT to be viable in South Africa because portfolio managers were able to manage their portfolio actively. In South Africa, the different UT funds are managed by different portfolio managers as opposed to other countries where all the UT funds are managed by one portfolio manager (Newsman, 2002).

1.1.2. Profitability of Unit Trust Companies in Kenya

ROA gives significant information regarding profitability however, what interests unit trusts investors is their investments earnings. ROE measures this, that is net income generated per dollar of capital. Kagunga (2010), describes unit trust performance as ability of a UT company to achieve its established goals. Evaluating the performance of a company is significant because it determines if portfolio managers have made gains on money invested by unit trusts investors.

Return on Assets (ROA) measures extent on how assets have been utilized to obtain gains. Higher Return on Assets (ROA) indicates good financial gains, attributable to higher rate of return on investment (Riyanto, 2001). According to Harahap (2002), ROA is the capacity of the firm to earn profits during particular time range. In their study Kosmidou, Pasiouras, & Tsaklanganos (2007) reveals, ROA is the key ratio for determining profitability and it used by many companies to

determine company's profit. As stated by Sofyan (2001), return on equity (ROE) indicates what percentage of net income is gained relative to investor's capital. The greater the profits, the greater the returns. Higher corporate returns cause increase in stock prices therefore increase in the number of investors who will buy more of the company's shares.

According to Willie and Hopkins (2007), the most accurate way to determine a company's financial power isn't the asset size, branches or technology investment but it's ROA. ROA is a very desirable way for measuring returns. To determine profits of unit trust companies, ROA will be applied. According to a UT profitability study, China is estimated to increase its total assets under management to $11.8 trillion by 2050.China doesn't have a defined contribution plan that allows investors to participate in unit trusts. If a planning system is put in place, China is estimated to have $15 trillion of assets under management by 2050 (Kagunda, 2011).

As at June 2012, there were only 951 UT funds in Africa. Forbes by Alexander indicated that in South Africa the total assets were R3.2 trillion in 2012 as compared to R3.0 trillion in 2011 showing a six percent increase. World Bank shows a rise of 4.4% in January 2013 and expects the growth to be 4.9% in December 2013. The analysis further shows an estimated increase of 5.2% and 5.4% in 2014 and 2015 respectively (KPMG, 2013).

Unit trusts in Kenya commenced after the enacting and amendment of the CMA (Capital Markets Authority). These laws are under the capital markets act approval of 2001 that encourages investments in Kenya. Kenyans total assets ranged between Ksh 38.0 billion and 17.6 billion in 2013 and 2010 respectively.

UT industry in Kenya is still in its early stages. The first company in Kenya to establish UT was the Zimele Asset Management Company and was registered by CMA and RBA. The initiative for

them then was to pool resources together and come up with a substantial amount where they could invest in various interest-earning instruments like treasury bills, bonds, and commercial paper. They had three investment portfolios, an offshore portfolio which allows investors to invest in foreign companies, a balanced portfolio which combines both local and international markets and money markets which deal with short-term financial objectives like commercial papers (KPMG,2013).

In Kenya, the leading corporate trustee in the industry is KCB Limited which has 99% of unit trust common scheme customers including Old Mutual Unit Trust, CBA Unit Trust, British American, Sentra Unit Trust, Zimele, and Stanlib Unit Trust which collect monthly incomes for unit trusts (KCB Custody, 2010). The growth and profitability of UT companies has been steady but at a lower rate than what was expected. Just like any other business, the UT companies face some challenges like ruthless competition which make UT companies to fail almost immediately after their launch (Zimele, 2010).

1.1.3. Portfolio management and profitability

Kimeu (2010) while studying centum investments explored if momentum trading strategies tend to be rewarding as factors affecting financial performance in the Kenyan stock market therefore, he investigated its performance origins. Momentum portfolios are notably successful in Kenya, but profits from them become unimportant after adjusting for risk as per Chordia and Shivakumar (2001) model. Strategies focusing on the particular equity returns are scrutinized to test the part of overall yield that make securities to go into utmost portfolios. The model establishes that profits have an impact near to the one arrived by aggregate return momentum strategy.

Jeroz (2007) while studying investment firms endorsed funds to be assessed in addition to being modified regularly following industry trends. Jeroz recommended fund assessment should be based on risk and expected returns when managing portfolios so as to increase profits. The portfolios have to be adjusted according to market dynamics. He advocates funds composition in allotment of excess money available plus other financial assets. He mostly focused on the principles governing asset allocation.

E. Fama (2001) has studied the unit trusts portfolio manager's ability of selecting the stocks from the market and their market timing. He has suggested that the overall profitability of the managed portfolio be depended upon certain parameters and profitability can be broken down into several components like those that one of them is market timing in the market price movements. These studies emphasize on the market timing expertise of the portfolio managers in choosing the securities. Fama has argued that the returns of the fund are not only fully dependent on the portfolio manager's ability of selecting the best securities at a particular risk level but also part of the expected returns also arise due to the prediction of selecting the securities with the correct market timing.

Ross M. Miller (2005) studied the unit trusts and tried to focus on management fees charged by the UT companies. He established that unit trusts are little bit expensive than what investors are commonly believed or what the funds tries to show to the investors. The management fees are charged on the two categories like Active management and Passive management. The actively managed funds are more expensive than the passive managed funds. However, UT companies are trying to combine both in the same case, so that the active management funds should not seem to be more expensive.

Stanley B Block and Dan W. French (2000) have studied weight allocated to the security in the fund and fund value weighted for the security. The study tried to research on one of the parameters of UT profitability that is weight allocation for the security. The selected actively managed unit trusts showed that funds are equally weighted to a higher degree than they are value weighted, meaning that investment performance based only on a single value-weighted benchmark may not sufficiently identify excess profits.

1.1.4. Unit trust Companies in Kenya

Capital Markets Authority is a government regulator overseeing grant authorization and regulating capital markets in Kenya. The capital markets in Kenya offer a variety of investment options like equity shares, government bonds and unit trusts. A product selected by an investor depends on her investment plans, duration and investor's funds. It is only recent that UT have gained popularity. This is backed up by increase in unit trust companies from no players in 2001 up to eleven in 2008. Unit trusts enables small-scale investors in achieving diverseness with little capital (CMA, 2003).

The average UT annual growth was Sh1.9 billion to Sh17.6 billion during the last nine years which is lower as compared to other business in the finance arena like pension funds whose growth for the last five has been from Sh176 billion in 2005 to Sh420 billion. UT companies tend to invest in less riskier securities like bank deposits and equity stocks (CMA, 2010). All unit trusts companies in Kenya are located in Nairobi the Kenyan Capital city and offer Money Market, Bond, Balanced and Equity Funds. Example of companies which offer UT products are UAP Old Mutual, Britam, CIC and Madison.

1.2. Statement of the Problem

Over the last few years, several unit trusts companies in Kenya have reported many cases of low profits as a result of reasons not yet uncovered. According to the report by CMA (2017), the number of investors investing in UT has reduced and existing investors are pulling out their funds. From the same report on the analysis of UT profitability, it established a diminishing rate of return. The rate is 5.5% for some UT companies while others are 9.8% (Cytton, 2018). From the aforementioned statistics it clearly tells that the UT companies are not well performing and may be associated with portfolio management.

According to Nicoll (2005), UT makes sense to investors when rate of return is more than the inflation rate and the securities exchange and if return from UT is more than that of the underlying assets. Lambrechts (1999) reveals that unit trusts are viable if they increase company profitability and adds shareholder's wealth. However as from 2010, UT companies have faced a decline in their rate of returns which has over time been associated partly to making investment decisions with the approval of their trustees who are banks and are not the best suited to be trustees in complex financial products, hence this restrains the market to plain vanilla investments such as bank deposits and government debt (Cytton, 2018).

The decline in profitability of UT companies has been majorly associated with portfolio management, low returns, investors perception of risk and illiquidity.This has led to introduction of regulations by the Capital Markets Authority. Improving fund transparency by portfolio managers in order to provide investors with more information where each Unit Trust company should be required to publish their portfolio holdings on a quarterly basis. Q3'2020 saw investors in Amana Capital, whose funds had been frozen for the past 2 years, receive a 59.0% impairment on their investments following the losses incurred from investing in the Nakumatt commercial

paper, yet they were not aware that their funds had been invested in the Commercial Paper (Cytton, 2020)

This area is a key player in the economy, as it holds KES 88 bn of investor' s money but not many specialists have inquired about the immediate connection between portfolio management and profitability of unit trust companies. This study therefore seeks to investigate the relationship between portfolio management and profitability of unit trust companies in Kenya.

Studies done in Kenya include: Karimi (2013), who studied the risk minimizing portfolio at the NSE, Kamwaro (2013) analyzed a heuristic exploration of portfolio performance measures by pension portfolio managers plus difficulties they deal with while managing portfolio in Kenya and Karanja (2012) researched factors influencing investment company portfolio choice. Sallah (2005) studied portfolio returns utilizing divergent portfolio management methods in LUSE and Obusubiri (2006) researched corporate social responsibility & portfolio performance in JSE. Jasmin (2010) concluded investing is main trade undertaking for almost all companies in the United Kingdom.

Asset allocation decisions by portfolio managers relative to unit trust profitability is not a widely researched area in Kenya. Kagunda (2011) investigated the asset allocation decision by portfolio managers and its impact on performance of equity funds hence was able to attribute performance. Peter (2010) in his study attributed that the reason unit trust outperforms the market is because portfolio managers can foretell equity prices due to characteristics such as market capitalization, price earnings ratios and price to book value ratios significant to the funds. As a researcher I find there's a study gap as previous studies did not focus on portfolio management and it should be filled by researching portfolio management and profitability of unit trust companies in Kenya.

1.3. Objectives of the study

1.3.1 General objective

To establish the effects of portfolio management on the profitability of unit trust companies in Kenya.

1.3.2. Specific Objectives

The specific objectives guiding this study include:

i. To establish the effect of expected returns on profitability of unit trust companies in Kenya.

ii. To establish the effect of risk on profitability of unit trust companies in Kenya.

iii. To establish the effect of liquidity on profitability of unit trust companies in Kenya.

1.4. Research questions

The study sought to answer the following research questions:

i. What is the effect of expected rate of return on profitability of unit trust companies in Kenya?

ii. What is the effect of risk on profitability of unit trust companies in Kenya?

iii. What is the effect of liquidity on profitability of unit trust companies in Kenya?

1.5. Significance of the Study

Insights provided will be worthy of attention to investors, unit trust companies and policy makers in the unit trust industry. The government through regulatory bodies like NSE and CMA may use the insights provided to develop new policies and regulations to boost profitability in the unit trust industry and enable Kenya to achieve vision 2030.

Research and Development are important in an economy. The findings established here will contribute towards the knowledge gap which may be used by subsequent researchers and academicians on related topics hence it may a reference point of future studies. This study will help financial performance analysts to carry out research on unit trusts profitability and determine factors affecting profitability of UT companies. Findings from this study may assist financial analysts to analyze market and advise current and potential investors.

1.6. Scope of the Study

The study centered on portfolio management and profitability of unit trust companies in Kenya. The study aim was to establish factors asserting influence on profitability of unit trusts companies in Kenya. This study collected data about portfolio management from portfolio managers in Kenya. Although the literature identifies various factors affecting profitability of unit trust companies, this study focuses on how portfolio management affects profitability of unit trusts companies in Kenya. The population were portfolio managers from UT companies in Kenya registered by CMA who provided a workable base. The study was conducted it the months of August 2020 to November 2020.

1.7. Limitations of the study

Some limitations were experienced during this study. Targeted participants comprised of business organization management with strict schedules. To mitigate this challenge, questionnaires were administered electronically. The targeted participants were also hesitant to respond to some of the contents of the questionnaire. This is because business responses on strategic position and performance variables maybe expose sensitive company information that could jeopardize the competitive position of the firm if shared irresponsibly. In order to overcome this limitation, the researcher attached a personal commitment letter providing that the data would be handled with

uttermost confidence and would not be divulged to third parties. Authorizations from Kenyatta University and NACOSTI were attached to guarantee respondents on the purely academic goal of the study.

1.8 Organization of the study

The project is organized into five chapters. Chapter One covers the background, statement of the problem, objectives of the study, research questions, significance of the study, scope of the study, limitations of the study and organization of the study. Chapter two details the theoretical and empirical literature, the third chapter covers the research methodology which includes, research design, target population, data collection, validity of the research instrument, reliability data analysis and ethical considerations. Chapter four presented the study findings and discussions while chapter five includes summary of findings, conclusions and recommendations.

CHAPTER TWO

LITERATURE REVIEW

2.1. Introduction

This chapter covers literature review where theoretical review alongside empirical review research gap and conceptual framework are explained.

2.2. Theoretical Review

This study examined theories which are relevant in explaining profitability of unit trust companies in Kenya. The theories enable the study to pin out factors that explain profitability of unit trusts companies, portfolio management, expected rate of returns, risk and liquidity. The study was steered by Modern Portfolio Theory, Financial Intermediation Theory and Capital Asset Pricing Model.

2.2.1. Modern Portfolio Theory

Modern portfolio theory was introduced by Harry Markowitz in 1952. It is a portfolio construction theory that determines the minimum level of risk for an expected return. MPT is an investment ideology that seeks to boost portfolio expected income given certain risk level or minimizing risk given specific objective of expected income, by selecting assets proportionally. (Markowitz, 1959).

Modern portfolio theory and capital market theory have transformed investment management through enabling portfolio managers to assess the risk and expected returns of a portfolio

The two theories points that portfolio risk and not individual asset risk should be the focal point of portfolio managers. One can mix a risky asset and come up with a portfolio whose expected returns reflects the asset mix but at a lower risk level (Fabozi & Grant, 2001).

MPT assumptions have been questioned. MPT reasons investors to be disinclined to risk, suggesting investors prefers less risky portfolios if they are made to choose portfolios that have the same expected returns. This means an investor will pick a higher risk if it offers a higher return. Therefore, investors preferring higher yields assume further risk. Different investors analyze risk differently based on their risk aversion perception. Therefore, a rational investor will pick a portfolio with conducive risk-expected yields. MPT is a form of diversification. MPT breaks down on how to establish the ultimate diversification strategy (Brodie, 2009).

MPT has various criticisms; its simple assumptions being the main ones. Critics cross examines its feasibleness as investment action plan, since it is not applicable in reality; risk, yield and parallel considerations utilized by MPT rely on forecasted future estimates. Key to portfolio theory is the evaluation of link uniting risk and return and assuming investors should be remunerated for taking risk (Reilly & Brown, 2009). Modern Portfolio Theory was examined to expound the aspect of risks and returns in investments involving unit trust funds in Kenya. Behavioral economics has challenged the MPT assumptions because MPT doesn't regard personal, environmental, strategic, or social facets of investment determination. The major focus is on risk-adjusted returns alone (Rani, 2012). MPT theory is an advanced outlook that helps investors to cluster, approximate and direct expected risk and return; it is also referred to as Portfolio Management Theory.

2.2.2. Financial Intermediation Theory

Financial intermediation came about in the twentieth century and Gurley and Shaw (1960) developed it. The financial intermediation theory is grounded on informational asymmetry theory together with agency theory. Resource allocation is efficient and there is no contribution by intermediaries to create more value. Utilizing Modigliani-Miller, financial structure is immaterial because; households are able to create portfolios, that balance out intermediaries' action, and intermediation is not able to create any additional value (Fama, 2001). According to Allen and Santomero (2001) financial intermediation theory focuses on actual market characteristics like cost of transactions and information asymmetry.

Allen and Santomero (2001), reveal that financial intermediation theory tends to center on financial company's roles which may not be very useful across all financial companies in today's world. The assumption that the companies cut on the costs of transacting and asymmetric information is becoming less and less relevant despite being relevant earlier. Allen and Santomero then argue that the financial intermediaries assume risk which is transferred to the financial institutions from investors in addition to dealing with complex financial instruments and markets. Traditional intermediation theory did not consider the risk element. Furthermore, financial intermediaries lessen participation costs plus learning costs of electively using markets and educating them about any significant market happenings.

Financial intermediation lures investors to purchase securities backed by investments whose risks the investors cannot quite assess. An investor who purchases securities from the intermediary examines historical performance of the intermediary and risk that the securities carry. Unit trust companies offer services as intermediaries as they enable investors to own assets through them. If

an intermediary provides no services, investors can buy assets directly be it government bonds and equities directly and cut intermediary costs (Allen, 2001). Financial intermediation theory was adopted to describe the aspects of profitability of unit Trust.

Financial intermediation theory focuses on contributions by various financial intermediaries in economy. The existence of financial intermediaries is described by the facts of the following classes of elements: high transaction cost, timely and incomplete information and regulatory method (Green Baum, 2007).

2.2.3. The Capital Asset Pricing Model

CAPM was developed by Sharpe (1964) and Lintner (1965). CAPM is relevant to this day and it is applied in determining capital cost of companies and in performance measurement. CAPM expounds on the bargain between assets returns and assets risks, measuring assets risks as the covariance of its returns with returns on the market in general. The model suggests that the expected return of any two assets is linearly related to the covariance of the return on these assets with the return on the market portfolio. Every asset has a diversifiable or unique risk and non-diversifiable or market, risk.

It is important to establish how can CAPM attain its main objective, that is whether CAPM is able to spell out the relationship between risk and return relationship of assets. Many studies which were done earlier show that CAPM faces challenges expounding the past let alone predicting the future (Weber, 2006). CAPM is very crucial and it is applied in investment institutions like UT companies. CAPM enables portfolio managers to translate risk into estimates of expected ROE (Rossi, 2016).

The advantage of CAPM is its ability to provide strong and accurate forecast on how to estimate risk and its correlation with expected return. The formula is a theoretical representation of how financial markets price securities and calculate expected returns based on what investors have invested. CAPM also gives an approach for quantifying risk and approximating it to ROE. CAPM can approximate cost of equity that the model can yield. Portfolio managers utilize CAPM together with other tools plus their experience to come up with approximations and helpful cost of equity estimations. Despite the fact that CAPM is still arguable, modern financial theory is used in portfolio management (Rossi, 2016).

It is impractical to create a portfolio that has all securities (true market portfolio), any CAPM test which utilizes market proxy (e.g. FTSE 100, DAX, CAC 40) will test the specific portfolio as opposed to the **"**true market portfolio**".** CAPM is mainly applicable for single period, although it is applicable for multi period, but its assumptions decrease in reliability. CAPM doesn't include transaction costs**.** The betas that are applied in CAPM are the ones which are taken over various observations and are all linked to the past and therefore they cannot be fully depended on while making investments decisions. CAPM also works well in efficient market and if there are any imperfections in the market the specific risks will not be eliminated from the investment portfolio (Richard Roll, 2017).

2.3 Empirical Review

This study assessed a number of global, regional, and local previous studies that the study found applicable. Literatures relating to the independent variables for this study which include expected rate of returns, risk and liquidity have been discussed.

2.3.1. Expected returns and Profitability of unit trust companies

Investors are normally advised to put their money where there is minimum cost in tracking the benchmark (Alexander, Jones & Nigro 2001). Funds that generally underperform tend to have high expense ratios leading to less profits, successful funds don't necessarily grow profits by increasing fees but gain through increase in fund size (Et al 1996 & Carhart 1997), Equity funds that are actively managed ask for more management fees than funds which tracks index or other UT funds, showing increased hiring cost of personnel to attain assorted strategy hence lowering the profits margin of UT companies (Et al, 1999).

Chan et al. (2001), investigated companies in Japan and noted variation in returns on Japanese stocks and found a relationship with the following variables; earnings yield, size, book to market ratio and expected rate of returns. This reveals that there exists an important relationship between the four variables and profitability of the companies in Japan (Chan et al., 2001).

Expected return variables tend to create a great effect on growth and profitability of various unit trusts portfolios. Unit trust funds which invests in stocks and shares are negatively influenced when real interest rates on government bonds, fixed and call deposits increase because investors exit equity fund and invest their funds in the instruments earning higher interest therefore adversely affecting the profitability of Equity fund causing losses due to fixed costs and UT in general (Fernando, Klapper, Sulla & Vittas, 2003). If individual investors can get higher gains on less risky securities most investors will avoid equity fund. Greater profits in equity fund as compared to real interest rates will bring more investors to invest in equity fund hence recording higher profits for unit trust companies (World Bank, 2003).

Lakonishok et al. (2004) reveals that size and P/B effects are as a result of investors overreacting and not compensating for risk assumed by the investor. Investors act on the information received in regard to the company on how the company is expected to perform or the outlook of the company in the future. As a result of this the company stock might be over - priced or under-priced. Kothari et al. (2005) debates that utilizing yearly historical beta as opposed to monthly returns gives a more solid relationship between return and beta. He also notes that the relationship between P/B and return as noted by Fama and French (2006) and others is over stated by survivor bias in the sample utilized and conclude: "our examination of the cross-section of expected returns reveals economically and statistically significant compensation (about 6 to 9% per annum) for beta risk".

Brink (2004) examined local equity unit trust funds which traded in JSE during 1984 up to 2003 and divided them to seven appraisal intervals. Active portfolios tracking FTSE/JSE All-Share Index were sampled and the mean, median, standard deviation and a Sharpe ratio were computed during the time span under observation. Brink concluded eventually the average investor would earn similar expected returns if she would have followed index fund four times out of the seven, investing in an index fund would have been the better option as it increases profitability of unit trusts funds due to reduced costs of research.

Gaining higher expected returns is pegged on investors risk perception. Diversification reduces risk which leads to more profits (Brouwer, 2009). Investor is able to choose a superior based on efficient frontier through applying Markowitz theorem. Choosing where to invest depends on satisfaction which is attained from various investment avenues (De Brouwer, 2009).

Pokhariyal and Mwaura (2014) examined performance persistence of equity and blended unit trusts companies in Kenya. His research focused on establishing consistency of portfolio profitability from 2006 to 2009. The investigation gave exact proof that the fund size affected the profitability of a unit trust company because of cost decrease due to economies of scale. The decrease in costs leads to higher expected returns.

Returns are the earnings achieved by investors as a result of investing the funds. Returns can be classified as realized returns which we have received already or expected returns which we are yet to receive. Realized returns are calculated using historical data. Total returns refer to a return of the entire investment during a particular time and it includes capital gain (loss) and yield (Paulus Sugito, Irvan Noormansyah & Nursanita Nursanita 2017)

2.3.2. Risks and Profitability of Unit Trust Companies

Huang, Sialm and Zhang (2011) studied the risk shifting levels significantly of the unit trusts over time. They sought out the consequences of the shifting of risk levels of the UT funds. The study finds that there are various factors of the shifting of risk levels of the UT like ill motivated trades of portfolio managers to increase their personal compensation and sometimes they need to change their risks of the funds to benefit from stock selection and timing abilities. The researchers found that funds which increases risks records less profits and perform poorly than funds that maintain a constant risk level.

When regarding a portfolio with two risky assets: one yielding returns when it rains and one yielding returns when it doesn't rain; Sharpe (1963) reveals an investor with the two portfolio shall do well at all times and earn profits. Including a risky portfolio to another can decrease general

risk level in an all- round portfolio. Patel (2012) concluded putting funds in unit trusts is less risky as compared to investing in stock market. Unit trust funds are beneficial for small scale investors.

According to Murumba (2012), risk is very crucial to portfolio managers when investing. The riskiness of a portfolio is really important and influences the decision of investment managers. However, this doesn't mean that the riskier the investment, the higher the profits of unit trust companies.

In South Africa, UTs are distinguished by assets making the total UT fund and risk/reward outlook. Enabling UT firms to keep product uniqueness and suppress competition. Douglas (1998) pointed out four main risks facing UT in Nigeria and they are currency, liquidity, regulatory and human factor risk. Douglas (1998) recommended currency risk to be reduced through hedging strategies like forward contract, options, futures, swaps and money market hedging. This will ensure that the company achieves its profits target even when the market is down.

Douglas (1998) pointed that in Singapore unit trusts have the following risk exposures; currency, liquidity, regulatory and human factor risk. According to Jorion (2003), 45 percent of UT assets are invested in foreign currency assets, this increases currency risk vulnerability. Douglas (1998) recommended currency risk to be reduced using hedging strategies like forward contract, options, futures, swaps and money market hedging. This shows that a company can still achieve its profits targets when the risks are managed.

2.3.3. Liquidity and Profitability of unit trust companies

Liquidity is a ratio used to determine the ability of banks and financial institutions to meet short-term obligations when required to do so (Pandow, 2017). A higher liquidity ratio shows that the company is liquid. I describe market liquidity as how easily securities are traded. We can use the

word ease instead of cost. Trading costs comprises of commissions, fees and taxes in addition to bid-ask spread, trade price impact and costs as a result of movements in prices if trades can't be executed at once or when it is sub-divided into smaller trades. Bid ask spread is highly effective when measuring liquidity and it is readily available. There are two requirements that should be met when liquidity is under stress. The first one is showing the cost associated with closing a large position within a short time frame and the second one is it should be available at high frequencies (upper, 2000).

Omondi (2009) studied liquidity risk and portfolio management at centum investments explored liquidity shock effect caused by investors behavior in fund management in the period of financial crisis where there is no deposit insurance. He established investors responded to the liquidity shock by increasing their cash holdings by selling financial markets securities and not by dissolving bank loans. This shows that high liquidity affects positively the profits of UT companies because companies facing local financial woes changed asset liquidity through trading actively the securities in the financial market.

Oduwole (2015) studied liquidity premium, share restriction and unit trust performance in Nigeria. His research explored relationship between liquidity and UT performance applying return-based stale price measure to quantify assets liquidity in the portfolio. His research confirmed assets liquidity in UT portfolio affects profitability of unit trust companies. Moreover, the study indicated unit trusts with the highest liquidity has more investors therefore more profits in contrast to unit trusts with the lowest liquidity in Nigeria unit trust funds.

Foran and O'Sullivan (2014) studied Liquidity Risk and Performance of England unit trusts. They assessed liquidity risk as a characteristic of stock and as systematic liquidity risk, in England unit

trusts profitability. They found UK unit trusts ordinarily incline to equities with high liquidity with an exception of UT which have little equities. Nevertheless, equities which are highly liquid are priced better than equities which are illiquid. This shows that highly liquid securities are more profitable than illiquid securities. Their research showed major part of equity liquidity level and systematic liquidity risk in fund models for evaluating profitability.

Pastor and Stambaugh (2003) studied liquidity risk and expected equity profits in U.S.A during the year 1966 to 1999. They researched if market wide liquidity is a significant element in asset pricing. They exhibited expected equity profits are linked to profit sensitivity and total liquidity variations, their research showed liquidity is a wide and elusive concept which indicates ability to trade massive quantities quickly, cheaply and with minimum price interruption.

Ferreira et al. (2012) studied determinants of unit trusts profitability in 27 countries during 1997–2007 periods. His research found out unfavorable results in United States of America is because of liquidity constraints encountered by portfolios because they are obliged to put funds in local securities. Money invested in countries with liquid equity markets and well-structured regulations perform better and record more profits. Indeed, In the USA funds that are placed in small and illiquid securities record less profits to the scale, however this doesn't apply to funds outside the USA.

2.3.4. Profitability of Unit Trust Companies

A company needs to make profits to ensure that it remains a going concern because that way a company attracts and retains clients and new investors and it is likely to remain in business for a long time (Farah & Nina, 2016). As ways to increase company's profitability, the company's

management look for strategies so as to reduce costs and increase revenues to ensure that the net profit is high (Schreibfeder, 2006).

According to (Ofili 2014) actively managed unit trusts are more likely to achieve higher returns and hence more profits especially where the market is inefficient. Opting for passive portfolio management when the market is efficient enables UT companies to make more profits. (Jeroz ,2007) while researching UT companies advocated appraisal of portfolio management periodically to match and to be aligned with the current market needs in order for the unit trust companies to make profits. He further suggested that the appraisals should focus on the risks and returns associated with the investment. Fund portfolio allocation should also be altered and adjusted as per the altering market conditions in order to ensure that the fund's returns remains high.

Nicoll (2005) reveals that unit trust makes sense if their expected rate of return is higher than inflation rate and performs better than other assets in question. Woodlin (2003) debates that UT are practical if the portfolio is greatly diversified and the portfolio managers are managing it actively. On the other hand Lambrechts (2019) reveals that UT makes sense if they make the profits for the company and increase wealth for shareholders.

As stated by Mehrling (2005) in regard to efficient portfolio construction, various investments in a basket have to be combined and formed as a single portfolio. The expected returns from the portfolios are then calculated and portfolios are appraised by the various funds outcomes standard deviation. In lowering risk level, diversification is embraced and leads to increased profits of unit trust companies as shown in a study done by (Brouwer, 2009).

Goel (2013) studied about profitability of unit trusts and investors' behavior in India in the period between April 2006 to March 2012. His findings showed nearly fifty percent of unit trusts funds have a performance which is adjusted to risk (Sharpe ratio) which is low than set benchmark. He drew the inference saying players in unit trust industry who have invested their money decide on which unit trust product to invest based upon scheme's composition, scope, profitability, ranking and knowledge of portfolio managers. He advocated funds to adopt necessary steps in boosting profitability.

According to Los (2018), UT companies face liquidity challenges as a result of unexpected withdrawals which may lead to losses due to fixed costs. UT portfolio managers are aware of the liquidity risk that faces the company as a result of unexpected withdrawals because the Asian Financial crisis was a result of liquidity issues (Spaulding, 2007). Spaulding (2007) suggested that UT companies should put a certain amount of their funds in cash and near cash securities in order to tackle the liquidity issue and ensure that the company remains profitable.

2.3.5. Profitability of Unit Trust Companies in Kenya

Over the last few years, several unit trusts companies in Kenya have reported many cases of low profits as a result of reasons not yet uncovered. According to the report by CMA (2017), the number of investors investing in UT has reduced and existing investors are pulling out their funds. From the same report on the analysis of UT profitability, it established a diminishing rate of return. The rate is 5.5% for some UT companies while others are 9.8% (Cytton, 2018).

From the year 2010, UT companies have faced a decline in their rate of returns which has over time been associated partly to making investment decisions with the approval of their trustees who are banks and are not the best suited to be trustees in complex financial products, hence this

restrains the market to plain vanilla investments such as bank deposits and government debt (Cytton, 2018).

The decline in profitability of UT companies has been majorly associated with portfolio management and has led to introduction of regulations by the Capital Markets Authority. Improving fund transparency by portfolio managers in order to provide investors with more information where each Unit Trust company should be required to publish their portfolio holdings on a quarterly basis. Q3'2020 saw investors in Amana Capital, whose funds had been frozen for the past 2 years, receive a 59.0% impairment on their investments following the losses incurred from investing in the Nakumatt commercial paper, yet they were not aware that their funds had been invested in the Commercial Paper (Cytton, 2020)

2.4 Research Gaps

Table 2.1: Summary of Literature Reviewed and Research Gaps

Author	Topic	Findings	Gap
Dawe, Pokhariyal, Mwaura, (2014)	Performance persistence of equity and blended unit trusts in Kenya.	For both equity and blended fund, there was evidence of performance differences which tend to persist over time suggesting that performance persistence existed during the time the research was done and therefore investors can utilize measures of past performance when making	The study did only focused on Equity fund and not the other UT like Money market fund, Bond fund and balanced fund.

		decisions to invest.	
Brink (2004)	Effect of political risk on investments.	Governments can monitor their own policy environment and take remedial action if necessary.	His research however did not cover other risks like market, liquidity, financial, interest rate risks.
Fernando, Klapper, Sulla (2003)	The global growth of unit trusts.	Capital market development (which promotes trust in the unit trusts market) and a good financial system were the major factors which contributed to the growth of	The study focused in the Asia region in the 1990s.

		unit trusts companies.	
Alexander, Jones & Nigro (2001)	Survey of investors who purchased unit trusts from banks.	Bank-channel investors are less financially literate than those investors purchasing funds through other distribution channels.	Their survey however did not cover how investors invests in UT companies directly.
Carhart (1997)	Persistence in unit trust performance.	Persistence in unit trust performance doesn't mirror efficiency in portfolio selection, however portfolio returns, low expenses and	The study did not focus on risk, liquidity and expected returns.

		transaction costs are major determinants of UT companies profitability.	
Brouwer (2009)	MaPT: alternative behavioral portfolio theory	Maslowian Portfolio Theory (MaPT), obtains similar outcome as behavioral portfolio theory but includes more fascinating cognizance because MaPT commences from investor's needs and it is more predictive as opposed to a	This study concentrated on on portfolio management and not expected returns, liquidity and risk.

		descriptive theory.	
Lakonishok, Shleifer, & Vishny (1994)	Contrarian investment, extrapolation, and risk.	The study reveals that value strategies give more profits as they exploit poor investors conduct as opposed to the fact that the strategies are riskier.	Their study focused on value strategies while our study focused on portfolio management.
Kothari (2009)	The effect of disclosures by management, analysts, and business press on cost of capital, return volatility, and analyst forecasts: A study using content analysis.	Negative disclosures from business press sources result in increased cost of capital and return volatility, and favourable	The study assessed effect of disclosures while our study considered aspects of portfolio management

		reports from media reduce capital cost and ensure that the returns are stable.	and Unit trusts in Kenya
Fama & French (2006)	Profitability, investment and average returns	Valuation theory says that expected stock returns are related to three variables: the book-to-market equity ratio (B_t/M_t), expected profitability, and expected investment. Given B_t/M_t and expected profitability, higher expected	The study focused on returns and did not focus on liquidity, risk and portfolio management.

		rates of investment imply lower expected returns. But controlling for the other two variables, more profitable firms have higher expected returns, as do firms with higher B_t/M_t.	
Huang, Sialm & Zhang (2011)	Risk shifting and unit trust performance	Funds that increase risk perform worse compared to funds with low and steady risk.	The study focused on education administration students' progress in portfolio management. our study

			focused on portfolio management targeting Unit trusts in Kenya
Patel (2012)	Comparative study on performance evaluation of unit trust schemes of Indian companies.	The study period is 1st January 2007 to 31st December, 2011. The results of performance measures suggest that most of the unit trust have given positive return during 2007 to 2011.	The study focused on India's unit trusts while ours focused on Kenya's unit trusts/
Jorion (2003)	The long-term risks of global stock markets	Risk is an important	The research only investigates the persistence of

		element while investing.	investment risk and did not focus on market, liquidity, financial, interest rate risk.
Pandow (2017)	Performance of Unit trusts in India	UT industry in India is growing but has not reached its full potential compared to first world countries. The major challenges facing the Indian UT industry are few investors, lack of product	This study focused on unit trusts in India while our study focused on unit trusts in Kenya.

		awareness and many individuals are not interested.	
Upper (2000)	How Safe was the 'Safe Haven'? Financial Market Liquidity during the 1998 Turbulences.	The market withstood a high turnover showing how important liquidity provision is.	The study considered liquidity in the German market while our study focuses on liquidity in the Kenyan market.
Omondi (2013)	Factors affecting the financial performance of listed companies at the Nairobi Securities Exchange in Kenya.	Leverage had a significant negative effect on financial performance, liquidity, company size and company age had a	The study focused on listed companies while our study focuses on unit trust companies.

		significant positive effect on financial performance.	
Oduwole (2015)	The Performance of Nigerian Unit trusts in the Period 2011	Unit trusts reviewed were on average not able to predict stock in such a way that they were able to perform better than the buy and hold stocks. Chances of a fund to outdo the predicted returns were also very minimal.	The study focuses on Nigerian unit trusts while our study focus on Kenyan unit trusts.

Foran & O'Sullivan (2014)	Liquidity risk and performance of UK unit trusts	On average UK unit trusts are tilted towards liquid stocks (except for small stock funds) liquidity as opposed to illiquidity in stocks is positively priced fund profitability.	Their study focused on UK liquidity risk while our study focus on Kenyan liquidity risk.
Pástor & Stambaugh (2003)	Liquidity risk and expected stock returns	Expected stock returns are related cross-sectionally to the sensitivities of returns to fluctuations in aggregate liquidity.	The study focused on liquidity risk and expected stock returns while Our study sought to analyze the profitability based on the

			portfolio management practices targeting Unit trusts in Kenya
Muya & Gathogo (2016)	Effect of Working Capital Management on The Profitability of Manufacturing Firms In Nakuru Town, Kenya.	Competitive aggressiveness has a significant positive relationship with organizational profitability	The study focused on general company profitability while our study focuses on profitability of unit trust companies in Kenya.
Niresh & Thirunavukkarasu (2014)	Firm size and profitability: Sri Lanka manufacturing companies.	There is no indicative relationship between company size and profitability	The study focused on profitability of manufacturing firms while our study focuses on

		of listed manufacturing firms.	UT companies profitability.
Ofili (2014)	Review of risk management techniques in mergers & acquisition.	. It is therefore imperative that the companies going into the merger carry out in-depth assessment of the transaction. They should thoroughly analyze every area of potential failure; analyze areas that they consider synergistic.	The study focused on risk in relation to Mergers and acquisition while our study focuses on risk in relation to profitability of unit trust companies.

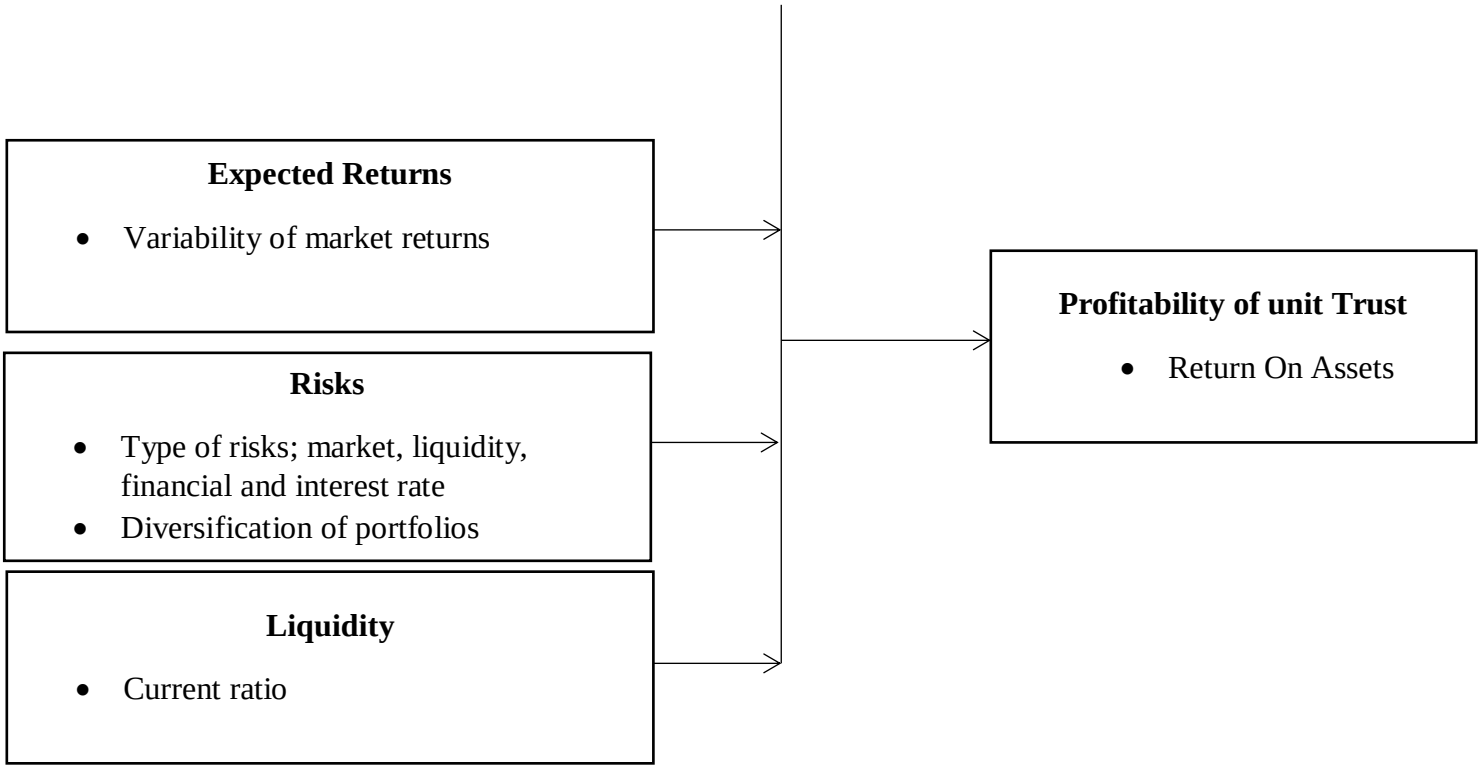
Source: Researcher (2020)

2.4: Conceptual Framework

According to Adom, Hussein and Agyem, (2018) a conceptual framework describes association between the study variables. Tamene (2016) argues that a study variable is a quantifiable aspect that assumes various outcomes in the subjects. A dependent variable relies on another variable such as independent variable. In this case profitability of unit trust companies is dependent variable while, portfolio management, expected returns, risk and liquidity are the independent variables.

Figure 2.1 indicates the relationship between the variables of the study. It sums up the independent and the dependent variables and how they relate to each other.

Figure 2.1: Conceptual Framework



Source: Researcher (2020)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1. Introduction

This chapter lays out study methodology. It provides particular approach heeded in pursuit of this study. The research design, population, sampling design, data collection methods and data analysis are set out in this chapter.

3.2. Research Design

Research design is a draft which lays out how a research will be done in order to come up with answers for the research questions (Suanders, Lewis & Thornhill, 2009). Research design helps to reduce errors and assist in utilizing data collection instruments and the techniques applied warrant research validity and reliability (Barasa, et al., 2015). The study took on descriptive analysis research design so as to commiserate profitability of unit trusts companies in Kenya from 2008 to 2018 financial years. Descriptive research design outlines current state of affairs. Mugenda and Mugenda (1999) reveals this study set describes possible behavior, attitudes, values and characteristics. Research design applied here was relevant as it helped to establish how portfolio management affects profitability of Unit Trust companies in Kenya and it ensured that the current state of affairs was well articulated.

3.3. Target Population

In statistics target population is hailed as particular group of people where particulars are derived. According to Ngechu (2004), population is a precise individual group of persons or object under

investigation. Focused population of this study are all the 96 portfolio managers of the twenty four unit trust companies in Kenya registered by CMA in June 2018.

3.4 Sampling Procedure

Sampling procedure means the way of coming up with a population. This involves ways in which the researcher will use in selecting items that will form a sample. The sampling procedure mainly incorporates taking samples and analyzing the sample with the objective of finding out something that can be connected to the entire population under study (O'Connor & Kleyner, 2011). Census study was adopted where all the population was included in study since population of target are all the portfolio managers of the unit trust companies since each unit trust company has four portfolio managers and resulted in a high degree of statistical confidence in the research.

3.5 Data Collection Instrument

Data collection instruments are tools which the researcher utilizes to get data after coming up with the research problem (Kothari, 2004). The researcher utilized primary data collected by means of structured questionnaire method so as to answer the research questions. Researcher sought for a research permit and sought for approval from the institution. Researcher then reached out to the respondents through a phone call or email then dropped the questionnaires plus a cover letter. Questionnaires also accorded respondents a privilege to give their contribution on the subject of the study (Phellas, Bloch and Seale, 2011). The researcher used secondary data checklist to review desired data contained in the portfolio management profitability aspects of Unit Trusts in Kenya. Pre-testing and expert opinion were employed with regard to validity and tool reliability was determined using Cronbach's Alpha coefficient.

3.5.1 Validity of Research Instrument

Validity describes how data collected represents the actual location of the investigation (Mohajan, 2017). Validity means, "Measure what is intended to be measured" (Taherdoost, 2016). Validity is expounded as capacity of test to measure what it professes to measure. Research instrument validation was done by pilot study application. Researcher tested internal validity to determine if explanation of a particular data or issue is actually sustained in actual data. The researcher also utilized content validity to make sure that research instruments fairly and comprehensively measures the items meant to be covered. Researcher used construct validity to measure if the theory and the construct correlates (Field, 2009)

3.5.2 Reliability of Research Instrument

Mugenda and Mugenda (2012), describe the reliability of a metal as a tool for researching to accurately measure the characteristics of anxiety over time. The small difference a tool that produces with standard quality standards grows greater reliability. To ensure reliability in the study, questionnaires were administered twice to the targeted unit trust companies business in Kenya at an interval of two weeks during the pre-test. The responses were used to assess the consistency of the study questionnaire (Hopkins, 2017).

The Cronbach's alpha was used in calculating the reliability and valued at 0.8 (Hair, Tahtam, Anderson &Black, 1998). The Cronbach's alpha values obtained for each variable was applied to determine questionnaire's consistency. Since Alpha coefficients obtained in this study were greater

than 0. It was concluded that the tool was reliable hence appropriate for this research. Cronbach's alpha values obtained are shown in the table below.

Table 3. 1: Reliability of study variables

	Factor	Cronbach's alpha
1	Profitability	0.912
2	Portfolio management	0.765
3	Expected returns	0.823
4	Risk	0.876
5	Liquidity	0.921

Source: Researcher (2020)

3.6 Data Collection Procedure

The researcher used to drop and pick the latter method to distribute these questionnaires to each of the respondents. This method ensured that respondents get enough time to fill in the questionnaires without interfering with their daily duties and responsibilities. The researcher used telephone calls, emails and short service messages (SMS) to remind the respondents on filling in the questionnaires. Questionnaires also accorded respondents a privilege to give their contribution on the subject of the study (Phellas, Bloch and Seale, 2011).

Secondary data was also be used as it is readily available and imperative in providing collective information to address the problem of the study. The researcher used secondary data checklist to review desired data contained in the portfolio management profitability aspects of Unit Trusts in Kenya. The secondary data collection perused journals and periodicals for the period between 2011 to 2020. This period is selected, as it is adequate to obtain current data, which shall be relevant for

the study. Pre-testing and expert opinion were employed with regard to validity and tool reliability was determined using Cronbach's Alpha coefficient.

3.7 Data Analysis and Presentation

Prior to processing responses, finished surveys were altered for culmination and regularity. Substance examination and clear investigation was utilized as well. Substance investigation was utilized to break down the respondents' perspectives. The information was at that point coded to empower the reactions to be gathered into different classes. Expressive measurements were utilized to condense the information including rates and frequencies. Tables and other graphical portrayals as suitable were likewise utilized to introduce the information gathered for simplicity of comprehension and investigation. Factual Package for Social Sciences (SPSS) variant 22 was utilized to break down the information. At that point results were relapsed to relate portfolio management and profitability of unit trusts companies in Kenya. The statistical model is shown below:

$$\mathbf{Y = \beta 0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_{3+} \varepsilon}$$

Whereby

Y = Profitability of unit companies in Kenya

$\mathbf{X_1}$= expected returns

$\mathbf{X_2}$= risk

$\mathbf{X_3}$= liquidity

$\beta 1, \beta 2, \beta 3$ = Coefficients of Determination

$\boldsymbol{\varepsilon}$ = Error Term.

$\beta 0$ = the minimum Y when the rest of the variables are held at a constant zero

3.8. Ethical Consideration

According to Saunders et al., (2009), ethical consideration should help researchers maintain standard behavior in the research. Ethical concerns were adopted and a letter of consent from the university was obtained. As an integral part of complying with ethical requirements, approval for this research from NACOSTI was acquired. Respondent's data was specified that it for academic purposes.

3.9 Operational and measurement of variables

The most vital part of an operational definition is measurement. The simplest meaning of measurement is putting figures to a variable in which we are interested. The figures furnish the raw material for our statistical analysis (Lammas & Badia, 2005).

Table 3:2 Operationalization and measurement of variables

Variable	Type	Operationalization	Indicators	Measurement
Profitability	Dependent Y	Capacity of businesses to make positive earnings given its current resources relative to other investments.	Return on Assets	A Likert Chart will be used to rank the level of performance, 1 shall be the lowest and 5 being the highest
Expected Returns	Independent X_1	Earnings which investors forecast in an investment with known or predicted return rate	Variability of market returns.	A Likert Chart will be used to rank the level of performance, 1 shall be the lowest and 5 being the highest
Risks	Independent X_2	Variability of returns on asset.	Type (market, liquidity, financial, interest rate,) Diversification	A Likert Chart will be used to rank the level of performance, 1 shall be the

				lowest and 5 being the highest
Variable	**Type**	**Operationalization**	**Indicators**	**Measurement**
Liquidity	Independent X_3	How fast a financial security can be traded at its current market price.	Current ratio	A Likert Chart will be used to rank the level of performance, 1 shall be the lowest and 5 being the highest

Source: Research data, 2020

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION

4.1. Introduction

This section lays out data analysis, presentation and its interpretation as per descriptive and inferential statistics. The study findings are set forth by use of frequencies, percentages, means, standard deviations, tables, graphs and charts.

4.2 Response rate

Portfolio managers in the 24 registered unit trust companies in Kenya were the study's population and sample. 80 questionnaires were filled out of 96 questionnaires giving an excellent 83.33% response rate. A response of at least 50% and above is effective (Mugenda and Mugenda, 2003).

Table 4:1 Response Rate

Response Rate	**Frequency**	**Percentage**
Response	80	83.33
Non-Response	16	16.67
Total	**96**	**100**

Source: Research data, 2020

4.2.1 Reliability Analysis

The study employed Cronbach Alpha in which a coefficient value of 07 and higher expressing that the tools used were effective. The table 4.2 presents the findings.

Table 4:2

Reliability Test

	Factor	Cronbach's alpha
1	Profitability	0.912
2	Portfolio management	0.765
3	Expected returns	0.823
4	Risk	0.876
5	Liquidity	0.921
	Average	**0.859**

Source: Research data, 2020

From Table 4.2 above, the Cronbach Alpha for profitability is 0.912, for portfolio management it was 0.765, for expected returns it was 0.823, for risk it was 0.876, liquidity had a coefficient of 0.921 while average alpha coefficient was 0.859. Cronbach (1957) indicates an alpha coefficient of more than 0.7 shows that the data collection instruments are reliable in measuring the study variables. Since all the coefficients of Cronbach Alpha were above 0.7, this indicates that the research instruments were statistically reliable.

4.3. Descriptive statistical analysis

Descriptive statistics are applied to summarize data in an arranged order by describing the relationship between variables in a sample or population (Yellapu, 2018). This section presents the general information on respondents' background and demographic characteristics. The study checked out work experience, number of years in the position held at the time of study, and the highest level of education of respondents as at the time of the study. The feedback were set forth in tables, charts, frequencies and percentages.

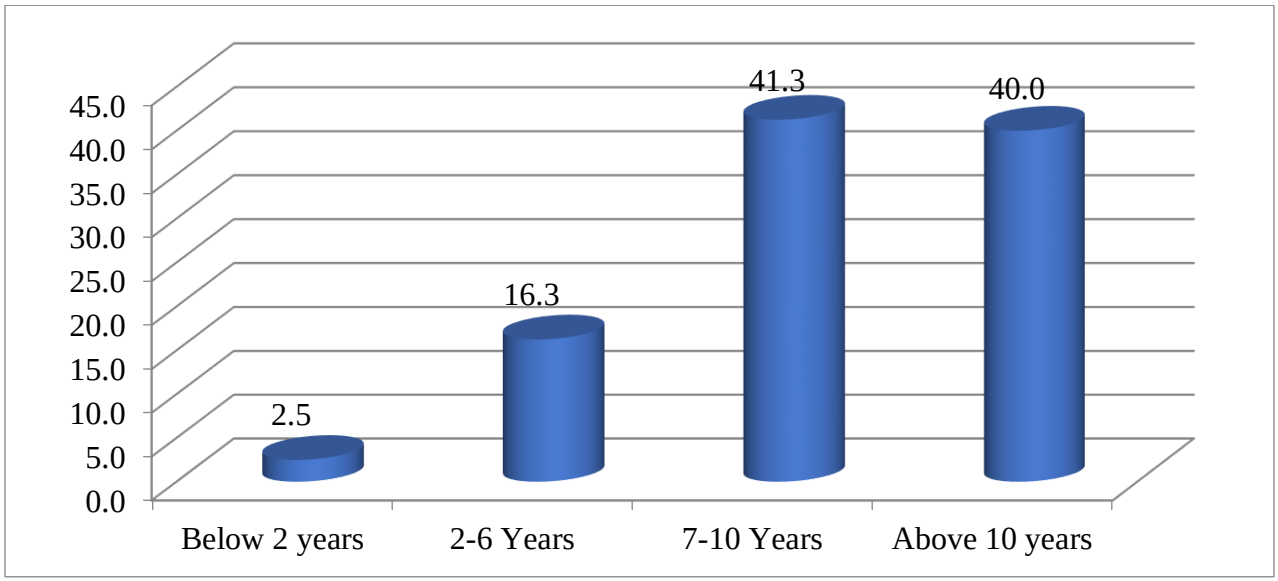
4.3.1 Respondents general information

As part of respondents' general information, work experience, number of years in the position held at the time of study, and the highest level of education attained by respondents as at the time of the study. This information provides basic understanding on the nature of persons involved in filling the questionnaires. Their profile is also an important aspect as their opinion in certain questions can be assessed based on this basic information. These findings are presented in the figure 4.1 and table 4.1.

4.3.2 Work experience

The study also sought to describe respondent's work experience; work experience is crucial basic information as work experience can influence the perception of respondents on the various factors and the extent of their effect on the profitability. The results are shown in figure 4.1 below

Figure 4. 1: Work experience



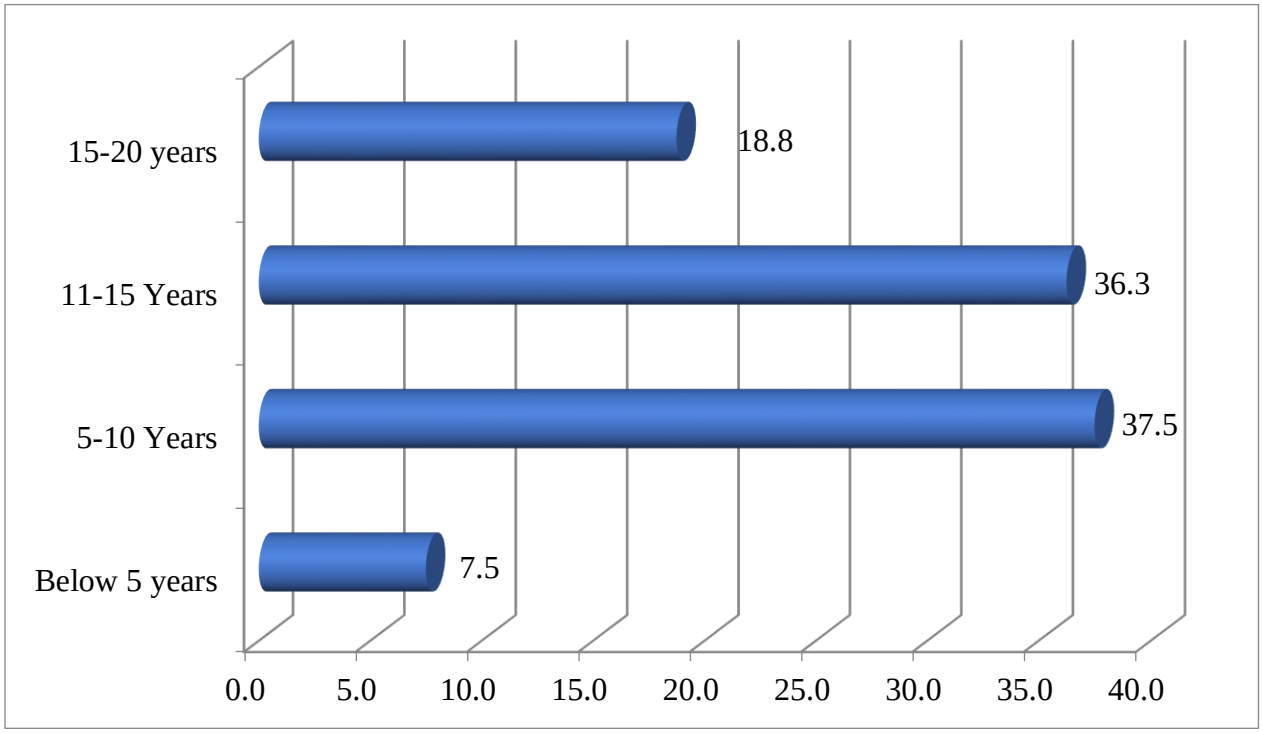
Source: Research data, 2020

The study found that most respondents had work experience of 7 -10 years (41.3%), a proportion that was followed closely by the respondents who reported a work experience of above 10 years. It was also noted that only 16.3% had 2-6 years' work experience and 2.5% below 2 yeas work experience. Generally, the finding implies that over 80% of respondents work experience was more than 7 years as at the time of this study (Figure 4.1).

4.3.3 Years worked in the position

The study further examined the respondents work experience in the same position served at the time of this study; duration served in a given position can influence the perception of respondents on the various factors and the extent of their effect on the profitability. The results is shown in figure 4.2 below

Figure 4. 2: Duration at current position



Source: Research data, 2020

The study found most respondents had worked in the same position for 5-10 years (37.5%). This proportion was relatively smaller than those who had worked for 11-15 years (36.3%) in the same position. It was also observed that 18.8% had worked in the same position for 15-20 years. This suggested that many respondents are knowledgable about the factors affecting profitability in the institutions that they represented.

4.3.4 Education qualification

The researcher sought information on the respondents' highest level of education attained and presented the results in Table 4.3 below. Education is an attribute of an individual that helps them to have a clear understanding of phenomena.

Table 4. 3: Highest education attained

		n	%
Highest education attained	Diploma	3	3.8
	Bachelor's degree	46	57.5
	Master's degree	27	33.8
	PhD	4	5.0
	Total	80	100.0

Source: Research data, 2020

Many respondents had at least a bachelor's degree as at the time of this study. The study found that majority had attained a Bachelors' degree level of qualification (57.5%), 33.8% had master's degree qualifications level while 5.0% reported to have attained a PhD level of qualifications as at the time of this study.

4.4 Descriptive Statistical analysis

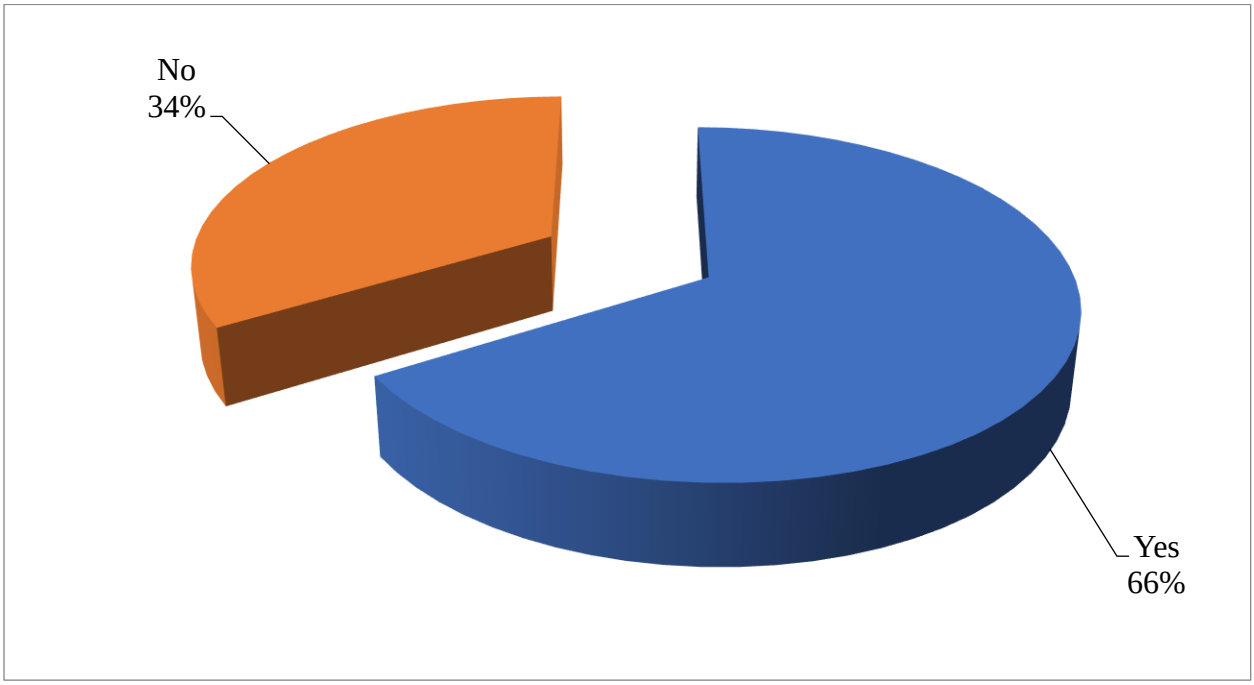
Descriptive statistics are utilized to summarize data in a orderly way by describing the relationship between variables in a sample or population (Yellapu, 2018). Descriptive statistics like mean and standard deviations were applied to show quantitative data together with Statistical Package for Social Sciences (SPSS) version 25. Descriptive statistics findings were based on study variables which include: expected returns, risk and liquidity and profitability of UT companies in Kenya.

The findings are presented as follows. Key: SA – Strongly Agree, A – Agree; N – Neutral; SD – Strongly Disagree, D – Disagree; M – Mean; SD – Standard Deviation.

4.4.1. Expected returns and profitability of unit trusts

The study assessed effect of expected returns on the profitability of unit trusts companies in Kenya. This is presented using figure 4.4, table 4.4 and table 4.5. Figure 4.3 presents the respondents general assessment of returns effects on the profitability. This response gives a general judgment of the respondent on the effect of expected returns on Profitability.

Figure 4. 3: perception on the effect of expected return on profitability



Source: Research data, 2020

Many (66%) respondents reported that expected rate of return affected the profitability of the unit trusts in Kenya. On the other hand, 34% reported that returns did not affect the profitability of the unit trusts in Kenya.

Table 4.4 presents the general overview of respondents' judgment on the extent that returns effected profitability of unit trusts in Kenya. Majority (51.3%) of the respondents said that expected returns effected profitability to a great extent. The second highest which was slightly large than those who reported that expected returns effected profitability to a moderate extent. However, approximately 70% of the management of Unit Trust felt that expected returns had ability to determine the direction of company profitability.

Table 4. 4: Extent of returns influence on profitability of unit trust

		n	**%**
Extent of returns influence on profitability of unit trust	No Extent	0	0
	Little Extent	5	6.3
	Moderate extent	19	23.8
	great extent	41	51.3
	very great extent	15	18.8
	Total	80	100.0

Source: Research data, 2020

Table 4.5 exhibits respondent's agreement level with a number of statements in regards to returns and their effect on the profitability of Unit trusts in Kenya. These aspects of expected returns include; "portfolio managers hope for higher expected returns as reward for assuming risk", "there is a relationship between portfolio expected return and individual asset expected return", "portfolio managers combine highest expected returns with the lowest risk for profit maximization", "investments that carry high expected returns and high risk don't attract many investors due to profit volatility" and "expected returns affect investment decisions as higher returns attracts more investors". These statements were assessed using 5-likert scale (1= strongly disagree, 2= Disagree, 3= undecided, 4= agree and 5= strongly agree) and findings presented in table below. The findings are also summarized using mean and standard deviation

Table 4. 5: Effect of Return on the profitability of unit trust

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	Std.
	n (%)	n (%)	n (%)	n (%)	n(%)		
Portfolio managers hope for higher expected returns as reward for assuming risk.	0(0)	2(2.5)	10(12.5)	35(43.8)	33(41.3)	4.238	0.767
There is a relationship between portfolio expected return and individual asset expected return.	0(0)	0(0)	11(13.8)	43(53.8)	26(32.5)	4.188	0.658
Portfolio managers combine highest expected returns with the lowest risk for profit maximization.	1(1.3)	8(10.0)	13(16.3)	40(50.0)	18(22.5)	3.825	0.938
Investments that carry high expected returns and high risk don't attract many investors due to profit volatility.	3(3.8)	3(3.8)	20(25.0)	38(47.5)	16(20.0)	3.763	0.945
Expected returns affect investment decisions as higher returns attracts more investors.	0(0)	15(18.8)	15(18.8)	31(38.8)	19(23.8)	3.675	1.041

Source: Research data, 2020

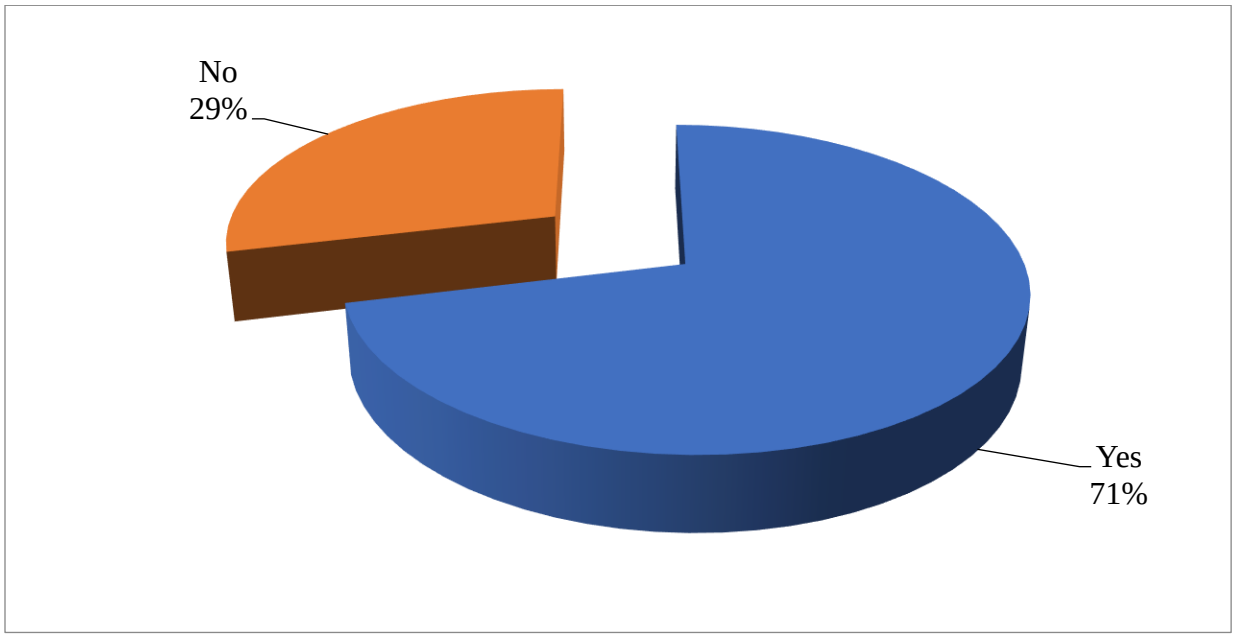
Most (43.8%=agreed) respondents felt that Portfolio managers hope for higher expected returns as reward for assuming risk. as implied by a mean of 4.238 and a standard deviation of 0.767. Respondents also reported there is a relationship between portfolio expected return and individual asset expected return. The study further found that Investments that carry high expected returns and high risk don't attract many investors due to profit volatility as implied by a mean of 3.763 and standard deviation of 0.945. Finally, on effects of return on the profitability of unit trust, the study shows that Expected returns affect investment decisions as higher returns attracts more investors indicated by a mean of 3.675 and a standard deviation of 1.041. The higher standard deviation shows high variability of responses while smaller standard deviation implies that respondents were more inclined to the mean response.

Lambrechts (1999), Woodlin (2003) and Nicoll (2005) did empirical research in order to expound on UT viability or success. Nicoll (2005), UT makes sense to investors if their rate of return is higher than the inflation rate and the securities exchange and if return from UT is more than that of the underlying assets. Lambrechts (1999) reveals that unit trusts are viable if they increase company's profitability and adds shareholder's wealth. This study confirms the above scholarly work that shows viability of the unit trust is based on the expected returns.

4.4.2. Risk and Profitability of unit trusts

The study assessed the effects of risk on profitability of unit trusts companies in Kenya. This is presented using figure 4.4, table 4.6 and table 4.7. Figure 4.4 presents the respondents general assessment of risk on the profitability. This response gives a general judgment of the respondent on the effect of risk on Profitability.

Figure 4. 4: perception of risk effect on profitability of unit trust performance



Source: Research data, 2020

Many (71%) of respondents reported that risk affected the profitability of the unit trusts in Kenya. However, 29% reported that risk did not affect the profitability of the unit trusts in Kenya.

Table 4.6 illustrates respondents' general overview in regard to their judgment on extent of risk and its effect on profitability of unit trusts in Kenya. Majority (55.0%) of respondents said that risk affected profitability to a great extent. The second highest which was slightly large than those who reported that risk affected profitability to a moderate extent. However, approximately 70% of the management of Unit Trust felt that risk had ability to determine the direction of company profitability.

Table 4.6: Extent of risk influence on profitability of unit trust

		n	%
Extent of risk influence on profitability of unit trust	To no extent	3	3.8
	Little Extent	4	5.0
	Moderate extent	17	21.3
	great extent	44	55.0
	very great extent	12	15.0
	Total	80	100.0

Source: Research data, 2020

Table 4.6 reveal respondents agreement level with a number of statements in regards to risk and their effect on the profitability of Unit trusts in Kenya. Aspects of risk examined in this objective include risk influences portfolio choice decision because risk affects profitability of unit trust companies, investment in unit trust is less risky than investment in stock market due to profit stability, while investing, interest rates affects investment choices as they affect company's profit, changes in interest rates affects profits of units trusts and may alter portfolio managers decision and risk assessment of the investment opportunities has an effect on performance and profitability. These statements were assessed using 5-likert scale (1= strongly disagree, 2= Disagree, 3= undecided, 4= agree and 5= strongly agree) and findings presented in table below. The findings are also summarized using mean and standard deviation.

Table 4.7: Effect of risk on the profitability of unit trust

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	Std.
	n (%)	n (%)	n (%)	n (%)	n(%)		
Risk influences portfolio choice decision because risk affects profitability of unit trust companies.	0(0)	4(5.0)	13(16.3)	45(56.3)	18(22.5)	3.963	0.770
Investment in unit trust is less risky than investment in stock market due to profit stability.	0(0)	5(6.3)	18(22.5)	30(37.5)	27(33.8)	3.988	0.907
While investing, interest rates affects investment choices as they affect company's profit.	0(0)	2(2.5)	14(17.5)	31(38.8)	33(41.3)	4.188	0.813
Changes in interest rates affects profits of units trusts and may alter portfolio managers decision.	1(1.3)	2(2.5)	12(15.0)	34(42.5)	31(38.8)	4.150	0.858
Risk assessment of the investment opportunities has an effect on performance and profitability.	1(1.3)	3(3.8)	51(63.8)	14(17.5)	11(13.8)	3.388	0.819

Source: Research data, 2020

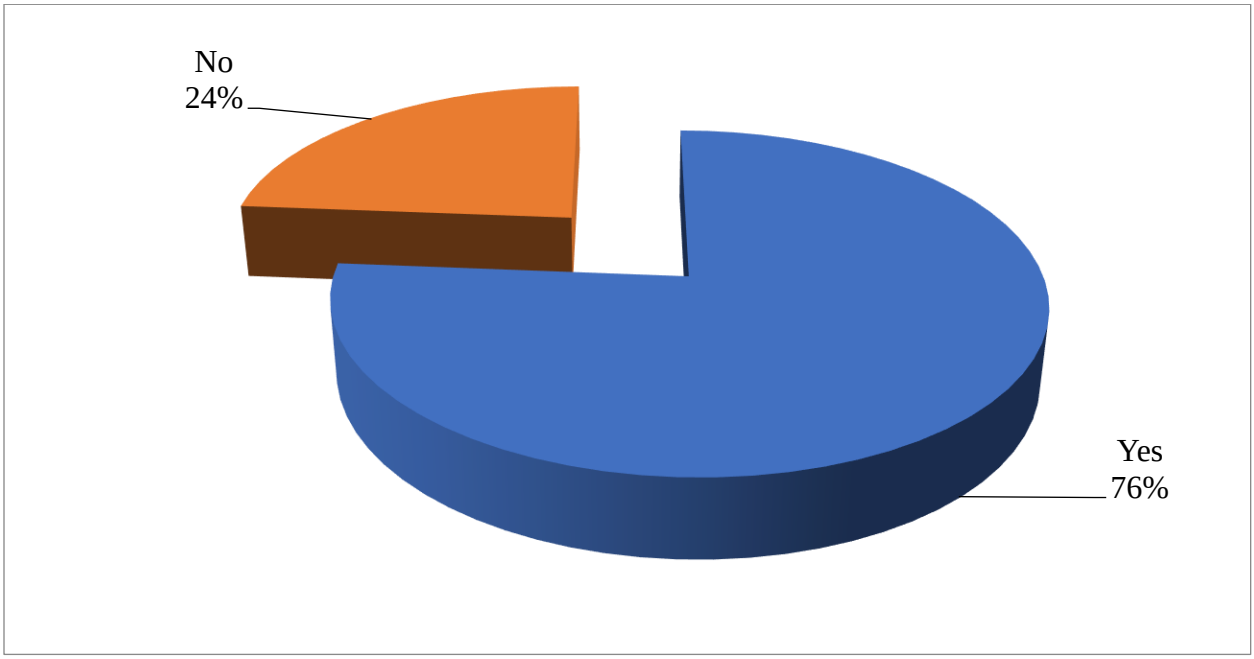
Majority of respondents concur that in choosing fund portfolio, risk influences portfolio choice decision because risk affects profitability of unit trust companies as implied by mean of 3.963 and standard deviation of 0.770. Respondents also agreed that investment in unit trust is less risky than investment in stock market due to profit stability. (mean=3.988 and standard deviation=0.907). The study further reported an agreement on while investing, interest rates affects investment choices as they affect company's profit.as implied by mean of 4.188 and standard deviation of 0.813. Respondents also agreed that changes in interest rates affects profits of units trusts and may alter portfolio managers decision as presented by mean of 4.150 and standard deviation of 0.858. Finally, respondents expressed uncertainty on risk assessment of the investment opportunities has an effect on performance and profitability as presented by a mean of 3.388 and standard deviation of 0.819.

Chen et al. (2004) investigated influence of risk in portfolio management of unit trusts profitability and found that the degree of focus on risk by management had a positive correlation with the fund's profitability. According to Dahlquist et al. (2000) who did a research on UT funds in Sweden which is a small market, the research showed a vital relationship between UT profitability and risk and this concurs with our study findings.

4.4.3. Liquidity and Profitability of unit trusts

The study assessed effect of liquidity on profitability of unit trust companies in Kenya. This is presented using figure 4.5, table 4.8 and table 4.9. Figure 4.5 presents the respondents general assessment of liquidity on the profitability. This response gives a general judgment of the respondent on the effect of liquidity on Profitability.

Figure 4. 5: perception on effect of liquidity on profitability of unit trusts in Kenya



Source: Research data, 2020

Most respondents (76%) reported that liquidity affected the profitability of the unit trusts in Kenya. However, 24% reported that liquidity didn't affect profitability of unit trusts in Kenya.

Table 4.8 show respondents' general overview in regards to liquidity's effect on profitability of unit trusts in Kenya. Majority (47.5%) of respondents said liquidity affected profitability to a great extent. Relatively smaller proportion (37.5%) that liquidity influenced the profitability of Unit Trusts. Generally, 85.0% of the respondents reported that management of Unit Trust felt that expected liquidity had ability to determine the direction of company profitability.

Table 4.8: Extent of Liquidity influence on profitability of unit trust

		n	%
Extent of Liquidity influence on profitability of unit trust	No Extent	0	0
	Little Extent	1	1.3
	Moderate extent	11	13.8
	great extent	38	47.5
	very great extent	30	37.5
	Total	80	100.0

Source: Research data, 2020

Table 4.8 presents respondent's level of agreement with a number of statements on the portfolio management and their effect on profitability of Unit trusts in Kenya. These aspects of liquidity include Portfolio managers create and apply liquidity financial models so as to influence profits, investors prefer unit trusts because they are highly liquid, and they are well diversified and liquidity preference affects the profitability of unit trust companies. These statements were assessed using 5-likert scale (1= strongly disagree, 2= Disagree, 3= undecided, 4= agree and 5= strongly agree) and findings presented in table below. The findings are also summarized using mean and standard deviation

Table 4.9: Effect of Liquidity on the profitability of unit trust

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	Std.
	n (%)	n (%)	n (%)	n (%)	n(%)		
Portfolio managers create and apply liquidity financial models so as to influence profits.	0(0)	0(0)	1(1.3)	16(20.0)	63(78.8)	4.775	0.449
Investors prefer unit trusts because they are highly liquid, and they are well diversified.	2(2.5)	9(11.3)	45(56.3)	19(23.8)	5(6.3)	3.200	0.818
Liquidity preference affects the profitability of unit trust companies.	1(1.3)	4(5.0)	7(8.8)	23(28.8)	45(56.3)	4.338	0.927

Source: Research data, 2020

Respondents strongly agreed that portfolio managers create and apply liquidity financial models so as to influence profits. (Mean=4.775 and standard deviation=0.449). Respondents reported general uncertainty on the view that the investors prefer unit trusts because they are highly liquid, and they are well diversified as implied by the mean of 3.200 and standard deviation of 0.818. Finally, on aspects of liquidity together with their effect on profitability, the study found liquidity preference affected the profitability of unit trust companies as shown by the mean of 4.338 and standard deviation of 0.927.

The results concur with those of Foran and O'Sullivan (2014) who in an analysis of Liquidity risk and the profitability of UK unit trusts found out that liquidity level and systematic liquidity risk have a strong effect on the unit trust profitability. Chang (2013) researched on liquidity and profitability of unit trust funds and found that liquidity influences unit trust companies profits. Bekaert (2007) revealed that liquidity measures is able to tell how the company is going to perform in the future. The effect of profitability and liquidity, credit, and solvency risks were examined and it was established that liquidity, credit, solvency risk had a negative effect on the unit trusts profits.

4.4.4. Profitability of unit trust companies in Kenya

The dependent variable of the study was profitability of unit trust companies in Kenya. Respondents were told to specify the extent to which they agree with the following statements in regards to the effect of portfolio management and profitability of unit trust companies in Kenya. These statements were assessed using 5-likert scale (1= strongly disagree, 2= Disagree, 3= undecided, 4= agree and 5= strongly agree) and findings presented in table below. The findings are also summarized using mean and standard deviation.

Table 4. 10: profitability of unit trust companies

	Strongly D...	Disagree	Neutral	Agree	Strongly Agree	Mean	Std. D...
		n (%)	n (%)	n (%)	n (%)		
Portfolio managers strive to maximize profits at the lowest risk.	0(0)	0(0)	6(7.5)	17(21.3)	57(71.3)	4.638	0.621
Portfolio managers seek opportunities in information asymmetry where data limitations on risk and return analysis present fundamental problems to the management of unit trusts.	0(0)	0(0)	22(27.5)	51(63.8)	7(8.8)	3.813	0.576
choosing the right combination of stocks promotes higher expected returns and increases the profitability of unit trusts companies	0(0)	0(0)	10(12.5)	30(37.5)	40(50.0)	4.375	0.700
Managing fund liquidity is a long term strategy that increases profitability of unit trust companies.	0(0)	5(6.3)	7(8.8)	59(73.8)	9(11.3)	3.900	0.668

Source: Research data, 2020

Majority of the respondents strongly agreed (71.3%) with the statement that Portfolio managers strive to maximize profits at the lowest risk as implied by a mean of 4.638 and a standard deviation of 0.621. It was demonstrated portfolio managers seek opportunities in information asymmetry where data limitations on risk and return analysis present fundamental problems to the management of unit trusts. as implied by a mean of 3.813(agree) and a standard deviation of 0.576. There was a general agreement on notion choosing the right combination of stocks promotes higher expected returns and increases the profitability of unit trusts companies as indicated by (Mean of 4.375 and standard deviation of 0.700). Consequently, managing fund liquidity is a long-term strategy that increases profitability of unit trust companies. by most respondents as indicated by a mean of 3.900(agree) and a standard deviation of 0.668. A low standard deviation in this study shows high level of agreement among the respondents on their responses.

4.5. Inferential statistics

Inferential statistics enables one to make predictions from data. With inferential statistics, you take data from samples and make generalizations about a population (Elst,2019). The study conducted inferential statistics to establish the extent to which portfolio management influenced profitability of unit trust companies in Kenya. Findings of Model Summary, ANOVA and Regression Coefficients are shown below.

4.5.1 Model Summary

The findings of coefficient of determination and coefficient of adjusted determination are as shown in Table 4.11.

Table 4.11: Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.935[a]	.873	.867	.01299

a. Predictors: (Constant), Liquidity, Portfolio management, Returns, Risk

The findings established that Coefficient of adjusted determination R^2 was 0.867 meaning a strong positive correlation between the variables. This means 86.7% of changes of dependent variable is a result of independent variables. 13.3% is as a result of variables not incorporated in this study. This coincide with a study by Murumba (2012) who established; expected returns, risk and liquidity are important determinants of profitability of unit trusts companies in Kenya.

4.5.2 ANOVA

The study carried out an ANOVA at 95% level of significance. The findings of $F_{Calculated}$ and $F_{Critical}$ are as shown in Table 4.12.

Table 4.12: ANOVA

ANOVA[a]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	0.087	4	0.022	12.9254	0.000[b]
	Residual	0.013	75	0.000		
	Total	0.100	79			

The findings show that $F_{Calculated}$ was 12.9254 and $F_{Critical}$ was 6.5241, this show that $F_{Calculated} > F_{Critical}$ an indicating that overall regression mode was significant to the study. The p value was 0.000<0.05 indicating at least one variable greatly influenced profitability of unit trust companies in Kenya.

4.5.3 Coefficients of Regression

Coefficient of regression was applied to determine individual influence of variables to project performance. Findings are shown in Table 4.13.

Table 4.13: Coefficients of Regression

Coefficients[a]					
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.165	.019		8.747	0.000
Returns	.011	.003	.152	3.308	0.001
Risk management	.055	.003	.818	16.871	0.000
Liquidity	.000	.004	.005	.110	0.913

a. Dependent Variable: Profitability

The resultant equation was

The regression model is; $Y=\alpha+\beta_1X_1+\beta_2X_2+\beta_3X_3+Ę$

$Y= 0.165+ 0.011X_1 + 0.055X_2 + 0.000X_3$

Where: X_1 = Expected returns

X_2 = Risk

X_3 = Liquidity

These findings implied that Unit trust would make a profit of around 0.165 units even when the expected returns, risk and liquidity are set at zero. Risk management was found to be the highest contributor to the profitability of Unit trust in Kenya followed by expected returns and finally

liquidity. This implies that the Unit trusts in Kenya can increase profitability more if they focused on enhancement of risk management as opposed to liquidity and expected returns. The study concludes expected returns and risk management were the significant predictors of profitability of Unit Trust companies in Kenya.

The findings pointed out that expected returns, risk and liquidity had a p value of less than 0.05 suggesting portfolio management greatly impacted profitability of unit trust companies in Kenya. Gatuhu (2011) concurs with the findings of this study: she researched on effect of risk management on financial performance of microfinance institutions in Kenya. She used descriptive survey design on all microfinance institutions in Kenya registered under Association of Microfinance Institutions and concluded a strong relationship exists between financial performance of microfinance institutions and risk management. Kalio and Kirui (2012) studied influence of risk management practices on performance of microfinance institutions in Baringo County also support this finding. They concluded a strong positive relationship between risk management and performance of microfinance institutions existed.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1. Introduction

This chapter shows summary of findings, conclusion and recommendations as per the findings and interpretation of variables in chapter four. Suggestions for further studies are brought forth too.

5.2. Summary of the findings

The study's aim was to determine the effect of portfolio management on profitability of unit trust companies in Kenya. Specific objectives were to establish the effect of expected returns, risk and liquidity on profitability of unit trust companies in Kenya. The study had a coefficient of correlation R of 0.877 showing a strong positive correlation between the variables and coefficient of adjusted determination R^2 was 0.867 which translates to 86.7%.

5.2.1. To establish the effect of expected returns on profitability of unit trust companies in Kenya.

On the expected returns, the study found majority of the respondents reported that expected rate of returns has an effect on the profitability of the unit trusts in Kenya positively. Most respondents also felt that portfolio managers look forward to getting good returns and increased profits as a reward for assuming risk while investing. Respondents also reported there exists a positive relationship between expected returns of portfolio and expected returns of single asset. The study further found that portfolio managers use conservative portfolio management style, combining the highest expected return and lowest risk level while investing so as to increase profits of unit trust companies. Finally, on effects of expected returns on the profitability of unit trusts, the study

found that expected returns was a significant element and had a direct positive relationship in an investment's profitability, if expected returns are high the more likely it is for investors to invest translating to higher profits for UT companies. The high standard deviation shows high variability of responses while smaller standard deviation implies that respondents were more inclined to the mean response.

5.2.2. To establish the effect of risk on profitability of unit trust companies in Kenya.

The study found many respondents reported that risk affected profitability of the unit trusts in Kenya. Majority of the respondents agreed that in choosing fund portfolio, risk influences decision-making. Respondents also agreed that UT investment is less risky than stock market investment thereby making unit trusts more profitable. The study further reported an agreement on importance of interest rates in investment decisions which affects positively company's profit. The changes in interest rates have an effect on the level of planned investment undertaken by portfolio managers as the changes has a positive influence in unit trusts company's profit. Finally, the respondents expressed uncertainty in regard to assessing investment opportunity risk has an effect on performance and profitability.

5.2.3. To establish the effect of liquidity on profitability of unit trust companies in Kenya.

Respondents reported that liquidity affected positively the profitability of the unit trusts in Kenya. The respondents strongly agreed that the portfolio managers utilized their exposure and resources to develop detailed economic liquidity analysis so as to increase profits. Respondents reported general uncertainty on the view that the investors prefer unit trusts as they are more liquid investment vehicles and forms a well-diversified investment portfolio because of their positive effect on profits. Finally, on the aspects of liquidity and their effect on profitability, the study revealed liquidity preference affected positively the profitability of unit trust companies.

5.3. Conclusions

This study concludes that portfolio management significantly and positively influenced the profitability of Unit trusts in Kenya. Portfolio management allowed one to invest in various assets while keeping risk low. The study also concluded that expected returns have significant and positive influence on the profitability of Unit trust. The study further concludes that risk has a significant effect on the profitability of Unit trusts in Kenya positively. Risk was perceived as one of key factor that influenced the decision making whether to invest or not. Though liquidity was found to be an insignificant to profitability, liquidity has positive association with profitability.

5.4. Recommendations

The study recommends units trusts should adopt portfolio management in making investment decision to increase their profitability. This can be achieved through adoption of active, passive and diversification of portfolio management. The study also recommends inclusion of expected returns, risk and liquidity when making investment decisions for their institutions. Organizations must be able to recruit team players with ability to comprehend return on the investment, relationship between the returns for a portfolio and single assets as well as combining highest return and lowest risk in arriving to decision making on a particular security. The study further recommends that portfolio managers to be equipped with ability to make decision on the on investments that involve high risk.

5.5 Suggestions for Further Studies

This study centered on portfolio management, expected returns, risk and liquidity on profitability of unit trust companies in Kenya. This study recommends other studies to focus on additional variables not studied as indicated by the coefficient of determination model which points out that

there are more variables that contribute to profitability of unit trust companies in Kenya which should form future research. The main objective of the study was to establish the effect of portfolio management on profitability of unit trust companies in Kenya, future research should be carried out on other factors to establish if there is correlation or not. The coefficient of adjusted determination R2 was 0.867; therefore, the residual of the study was 13.3% and can be explained by other factors beyond the scope of the current study that future scholars should focus on.

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APPENDICES

Appendix I: Questionnaire

Section A: General information

1. What is your gender.

Male [ ] Female [ ]

2. Number of years in the organization?

Below 2 years [ ] 2-6 years [ ] 7-10 years [ ] Above 10 years [ ]

3. Number of years in current position?

Below 5 years [ ] 5-10 years [ ] 10-15 years [ ] 15-20 years [ ]

4. What is your highest education level:

Phd [ ] Masters [ ] Bachelors [ ] Diploma [ ] Certificate [ ]

Section B: Portfolio Management and Profitability

6. Does portfolio management affect profitability of unit trust companies in Kenya?

Yes [ ] No [ ]

7. To what extent does portfolio management affect profitability of unit trust companies in Kenya?

To a very great extent [ ]

To a great extent [ ]

To a moderate extent [ ]

To a little extent [ ]

To no extent [ ]

8. To what extent do you agree with the following statement relating to portfolio management and profitability of unit trust companies in Kenya?

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Portfolio managers strive to maximize profits at the lowest risk.					
Portfolio managers seek opportunities in information asymmetry where data limitations on risk and return analysis present fundamental problems to the management of unit trusts.					
choosing the right combination of stocks promotes higher expected returns and increases the profitability of unit trusts companies					
choosing the right combination of stocks promotes higher expected returns and increases the profitability of unit trusts companies					

9. How does portfolio management strategy affects profitability of unit trust companies in Kenya?

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……

Section C: Return and profitability

10. Does return influences profitability of unit trust companies in Kenya?

Yes [ ] No [ ]

11. To what extent does return influences profitability of unit trust companies in Kenya?

To a very great extent [ ]

To a great extent [ ]

To a moderate extent [ ]

To a little extent [ ]

To no extent [ ]

12. What is you level of agreement on statement relating influence of returns on profitability of unit trust companies in Kenya?

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Portfolio managers hope for higher expected returns as reward for assuming risk.					
There is a relationship between portfolio expected return and individual asset expected return.					
Portfolio managers combine highest expected returns with the lowest risk for profit maximization.					
Investments that carry high expected returns and high risk don't attract many investors due to profit volatility.					
Expected returns affect investment decisions as higher returns attracts more investors.					

13. How else does returns influences profitability of unit trust companies in Kenya?

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Section D: Risk and Profitability

14. Does risk influences profitability of unit trust companies in Kenya?

Yes [ ] No [ ]

15. To what extent does risk influences profitability of unit trust companies in Kenya?

To a very great extent [ ]

To a great extent [ ]

To a moderate extent [ ]

To a little extent [ ]

To no extent [ ]

16. What is your level of agreement on statement relating to influence of risk on profitability of unit trust companies in Kenya?

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Risk influences portfolio choice decision because risk affects profitability of unit trust companies.					
Investment in unit trust is less risky than investment in stock market due to profit stability.					
While investing, interest rates affects investment choices as they affect company's profit.					
Changes in interest rates affects profits of units trusts and may alter portfolio managers decision.					
Risk assessment of the investment opportunities has an effect on performance and profitability.					

17. How does risk influences profitability of unit trust companies in Kenya?

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Section E: Liquidity and Profitability

18. Does liquidity affect the profitability of unit trust companies in Kenya?

Yes [ ] No [ ]

19. To what extent does liquidity affect the profitability of unit trust companies in Kenya?

To a very great extent [ ]

To a great extent [ ]

To a moderate extent [ ]

To a little extent [ ]

To no extent [ ]

20. What is you level of agreement on the following statement relating to effects of liquidity on profitability of unit trust companies in Kenya?

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Portfolio managers create and apply liquidity financial models so as to influence profits.					
Investors prefer unit trusts because they are highly liquid, and they are well diversified.					
Liquidity preference affects the profitability of unit trust companies					

21. How does liquidity affect the profitability of unit trust companies in Kenya?

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Thank you

Appendix II- List of Fund managers

	REGISTERED FUND MANAGERS - 2019
1	African Alliance Kenya Investment Bank Limited
2	Allan Gray Kenya Limited
3	Alpha Africa Asset Managers Limited
4	Altree Capital Kenya Limited
5	Amana Capital Limited
6	Apollo Asset Management Company Limited
7	Britam Asset Managers Kenya Limited
8	CBA Capital Limited
9	CIC Asset Management Limited
10	Co-op Trust Investment Services Limited
11	Cytonn Asset Managers Limited
12	Dry Associates Limited
13	Fusion Investment Management Limited
14	Genafrica Asset Managers Limited
15	Genghis Capital Limited
16	ICEA Lion Asset Management Limited
17	Kenindia Asset Management Company Limited
18	Madison Asset Management Services Limited
19	Nabo Capital Limited

20	Natbank Trustees and Investment Services Ltd
21	Old Mutual Investment Group Limited
22	Sanlam Investments East Africa Limited
23	Stanlib Kenya Limited
24	Zimele Asset Management Company Limited

Appendix III - Research Program

RESEARCH PROGRAM	
Turning idea into proposal topic	JANUARY 2019
Conduct a literature review	FEBRUARY 2019 - MARCH 2019
Design the study and develop methods	MARCH 2019 – APRIL 2019
Writing the research proposal	APRIL 2019 - JUNE 2019
Funding	JUNE 2019
Submit research proposal and seek approval.	AUGUST 2019 – MAY 2020
Collect and collate the data	JULY 2020
Analyze the data and interpret findings	AUGUST 2020
Report the project and disseminate the findings	AUGUST 2020

Appendix III- Research Information from Company Reports

		2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
STATEMENT	MARKET INFORMATION											
STATEMENT OF COMPREHENSIVE INCOME	Investment Income											
	Fund Management fees											
	Operating and other expenses											
STATEMENT OF FINANCIAL POSITION	Investment in fixed income securities											
	Income tax recoverable											
	Income tax payable											
	Paid up ordinary share capital											
OTHER DISCLOSURES	Minimum capital required											
	Future out look and strategies											
	Statement of compliance											
	Enterprise risk management report											
	Growth of Assets Under Management											
	Strategy report											
	Client age distribution											
	Fund invested distribution											