

**EFFECT OF MERGERS AND ACQUISITIONS ON THE FINANCIAL
PERFORMANCE OF THE COMPANIES LISTED AT THE NAIROBI
SECURITIES EXCHANGE**

**BY
MUNDE LENNOX MUTINDA**

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DECLARATION

I declare that this research project is my own work and it has not been submitted for any degree or examination in any other university.

Signature: Date:.....

Muinde Lennox Mutinda

D61/88231/2016

This research project has been submitted for examination with my approval as the University Supervisor.

Signature: Date:.....

Dr. Angela Kithinji

Lecturer

School of Business, University of Nairobi

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DEDICATION

This Research Project is dedicated to my parents Mr and Mrs Muinde, my wife Kellen Nyaga, my sons Steve Lennox & Leon Muinde Lennox, my daughter Natalia Koki Lennox, and my brother Lawrence Wambua for their support.

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LIST OF ABBREVIATIONS

DPS	Dividend per Share
EVA	Equal variances Assumed
EVNA	Equal variances not assumed
EPS	Earnings per share
M&As	Mergers and Acquisitions
NPV	Net Present value
NSE	Nairobi Securities Exchange
ROA	Return on Assets
ROE	Return on Equity

ABSTRACT

Companies that are doing well financially look for ways of improving their financial performance. These firms may target increasing their operations to other more or equally profitable industries or sectors of the economy. The most logical and appropriate way of making entry into a new sector, is by acquiring or merging with a company that already exists in the sector. This saves time and resources required to set up a new venture with no prior experience. M&A are therefore seen from the point of view of improving the financial performance of a smaller company. This is because it increases the asset base of the company increasing free cash flow that would be required in making investments in projects with positive NPV. This study therefore undertook to look at the effects of M&A's on financial performance of companies listed at the NSE. The study used a descriptive research design and secondary data on financial performance measured by profitability ratio, liquidity ratio, capital structure ratio and free cash flow ratio was collected from audited financial statements of 15 companies that had all necessary data for a period of 3 years before they merged and 3 years after the companies merged. Data collected was analyzed by the use of independent test of sample means that looked at the differences between the means of these variables for the companies before merger and after merger. Diagnostic tests of normality and Levene's test of equality of variances was undertaken. The findings were that the mean profitability of the companies after merger was greater than the mean profitability before merger. Similarly, the mean of capital structure and free cash flow was also greater after merger than before merger. However, the debt/equity ratio had mean before merger being greater than mean after merger. However, the t statistical test for equal sample means had a p value greater than alpha value for all the variables which meant that the study failed to reject the null hypothesis. It therefore implied that the financial performance of companies listed at NSE had equal means before and after M&A. There was therefore no significant effect of M&A on financial performance for the companies listed at NSE. This means that the study failed to reject the null hypothesis. It is therefore concluded that the difference in means of financial performance of companies listed at NSE before merger and after merger are not statistically significant. The study concludes that despite slight increases on financial performance for the companies after merger and acquisitions such increases are not statistically significant. This means that companies do not improve their financial performance by engaging in M&A. More synergy and approach is needed to enhance financial performance of these firms listed at NSE. The study recommends to the policy makers and regulatory authority to make provisions that would require companies engaging in either mergers or acquisitions to ensure that they set performance limits that would enhance financial performance of these companies after merger and acquisitions.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

A merger is the consolidation of equal strong companies aimed at forming a completely new company. The new entity formed lose their original identity after the combination and dominates the latter (Ruback, 2005). Combination of two or more firms is seen as a strategic move firms take to increase their value by consolidating their resources. An acquisition occurs when one business entity called the predator takes control over another business entity called the target (Ruback, 2005). The idea behind mergers and acquisitions is risk diversification which is normally achieved through conglomerate merger especially where the returns of the two firms are negatively perfectly correlated.

In the recent times, mergers and acquisitions have gained corporate concern due to its significance. Mergers and acquisitions have necessitated the maximization of the returns of the shareholders (Scholes, 2009). Business entities have achieved short term growth and this is made possible where the target is experiencing growth and profitability problems such a target can be acquired by the predator which will improve its financial performance hence increased profitability. Mergers and acquisitions aims at limiting the competition through empire building where mergers and acquisitions are motivated by the resultant gains. After the merger, the business entities involved will gain the market power (Sharpe, 2008).

Synergy is achieved through mergers and acquisitions. These are additional benefits associated with economies of scale after mergers and acquisitions. It is the creation of a whole which is greater than the sum of two combined business entities (Roll, 1988). Mergers and acquisitions are undertaken because they generate synergy according to the financial efficiency theory. Synergy implies a situation in which the value of the consolidated business entities is greater than the value of independent entities. This also arises from management capabilities, creativity and innovativeness (Ross, 2005). At NSE companies have undertaken mergers to expand their product offering and reach new markets. Capital markets is a critical sub-sector of “financial services” and the NSE is playing its significant role in attracting foreign capital through M&A and growing the domestic savings and investment rates to achieve its goals where M&A have contributed immensely. As of 31 December 2013, The Exchange had over 120 listed Companies for a total market capitalization of over Kshs 2.7 trillion (USD 31.18 billion) which was over 75% of Kenya’s GDP (NSE Prospectus, 2014).

The following theories relate to mergers and acquisitions; Monopoly Power Theory developed by Edwards (1955) implies that mergers and acquisitions are undertaken to realize monopoly power (Lambert, 2001). Empires building theory propounded by Marris, (1963), holds that mergers are planned and executed by corporate leaders who seek to optimize their own utility rather than the value of shareholders. Valuation theory or approach states that mergers are planned and executed by managers who are privy to more superior information regarding the target firm’s value compared to the stock market

(Ravenscraft and Scherer, 1987; Holderness and Sheehan, 1985; Steiner, 1975). Financial Efficiency Theory (Roll, 1980) which asserts that mergers and acquisitions create synergy. The efficiency gains accrue from operating synergies which are attained through the transfer of knowledge, economies of scope and economies of scale. These synergy gains are naturally not generic but rather peculiar to two specific firms that are merging (Mueller and Sirower, 2003) and on the other hand the Hubris Hypothesis (Brigham, 1980) which concluded that errors of over optimism are normally committed by managers during evaluation of the potential targets. The managerial hubris hypothesis opines that even if managers try to maximize the firm's value, the hubris compels them to overestimate the value of what to buy (Roll, 1986). The hubris theory provides a psychological-based approach on the issue of mergers. It argues that the acquiring firm's management overrates their ability to evaluate potential merger targets.

1.1.1 Mergers and Acquisitions

A merger is an act of consolidating business entities to form one business entity (Ross, 2008). Basically a merger aims at the creation of synergy, which are the benefits achieved as a result of mergers and acquisitions by different business entities where the financial performance of the individual business entities is less than the combined business entities. Many mergers involve the agreement by the parties involved, but some time the predator can forcefully initiate the process by influencing the management of the target company. Mergers are majorly by 2 ways, by seeking the support of the stakeholders of the target firm or using the tender offer by striking the deal directly to management of the target. Mergers assume three different groupings; either as are majorly categorized as

consolidation conglomerate and vertical mergers. Consolidations result from an alliance of more than two business entities in similar business. Conglomerate mergers is the alliance of business entities that do not operate in the same line of business. In addition vertical mergers is an alliance of two or more business entities at varying levels of the value chain or levels of production of different components, (Meshki, 1999).

An acquisition is a scenario in which one firm called the predator acquires another firm called the target firm. Usually, a larger company takes over the smaller company. Normally, the negotiations to takeover can be good or bad. If the business deal is good, the management of both business entities agree to work together towards achieving their goal but if is bad is likely to lead to poor financial performance since this is a forced deal. That means it was unfriendly and in such case the target company can resist the process by the use of the green mail where the target gets a counter offer to acquire the predator and the predator the target. This is possible where 2 firms are equally strong and can easily take over each other (Haley, 2001). These forms of business entities are vital because they help businesses achieve synergy from their resources. This however is possible only if confers some competitive edge to the firms. As a result of consolidations and acquisitions the entities achieve various benefits like quick accessibility of technology and products, improved market position and a healthy status financially. In addition, the businesses are able to venture into new geographical market more efficiently, to achieve more growth and expansion since they are able to capitalize on the benefits volume production or economies of scale like reduced costs of operation and increased customer portfolio amongst other reasons (Kemal, 2011).

1.1.2 Financial Performance

Financial performance deals with how prudent a company has used assets to realize income (Ross, 1995). It is normally over a specified period of time. It can be monthly, quarterly, semi-annually or annually. Measurement of financial performance is key to organizational success since all long term strategies are based on it. Financial performance is normally determined by the gearing ratios, profitability ratios and liquidity ratios. Liquidity ratios aims at establishing whether a company will be able to finance its short-term commitments, gearing ratios sheds more light on the degree to which debt financing has been employed by a business entity because debt financing also attracts the finance charge inform of interest rate. Profitability ratios aims at establishing how well the business entities have efficiently managed the resources to achieve their goals. The major goal of any business entity is to minimize losses and maximize the profits. This will ensure business continuity of business entities. Firm's financial performance is determined from the financial statements. Financial statements entail the financial reports of business entities.

Financial performance is a key measurement index of how the efficiency with which a business entity utilizes its assets from its primary form of business to generate revenue. The term is also used as a universal indicator of a financial status of an entire organization over a specified time period. This measure can be used to comparatively evaluate the performance of similar firms in the one industry or compare industries or aggregated sectors, (Gaul, 2011).

1.1.3 Mergers and Acquisitions and Financial Performance

These business entities are strategic alliances aimed at improving the financial performance of the business entities involved in the deal. Due to the increased competition in the business environment, mergers and acquisitions have emerged as the only survival tactic to gain competitive advantage (Graham, 2010). The monopoly theory, (Lambert, 1980) holds that these business entities are primarily formed or undertaken to achieve monopoly. Monopoly will improve the market share hence the market power. Dominance of a company will maximize on the profitability of that company as a result of high returns by limiting stiff competition.

Organization change in general but more specifically in the management structure is the most pronounced economic benefits resulting from mergers and Acquisitions. It enhances or improves organizational value which would not have been realized without a change in the organizational control (Pazarkis et al., 2006). Such changes in controlling or management structure are assumed to yield most benefits when they lead to the redeployment of resources, and a definition of a new strategic direction through development of new operational plans and formulation of new business strategies. The main goals of mergers and acquisition are to enhance revenues generation, increased profitability, quick growth in scale, shorter time to market, and acquisition of new technology. This is majorly the reasons attributable to the perception of these form of businesses as the best methods of improving organizational performance.

1.1.4 Nairobi Securities Exchange

The Nairobi Securities Exchange is the 4th largest securities market in Africa and it was founded in 1954. It is among the most active market for securities in the world. The Nairobi Securities Exchange has classified the listed companies into segment basis. There are 64 quoted firms on the NSE. (Nairobi Securities Exchange, 2014). Of these 63 companies quoted at the Main Investment Segment while one firm is quoted on the Growth Enterprise Market Segment. The following are some of the listed companies, equity group holding limited, Kenya Commercial Bank Limited, Stanbic Holding Limited, Co-operative Bank of Kenya, KenolKobil Limited, Total Kenya Limited, CIC Insurance Group Holding and Jubilee Holding Limited.

At NSE companies have undertaken mergers to expand their product offering and reach new markets. Capital markets is a critical sub-sector of “financial services” and the NSE is playing its significant role in attracting foreign capital through M&A and growing the domestic savings and investment rates to achieve its goals where M&A have contributed immensely. As of 31 December 2013, The Exchange had over 120 listed companies for a total market capitalization of over Kshs 2.7 trillion (USD 31.18 billion) which was over 75% of Kenya’s GDP (NSE Prospectus, 2014).

1.2 Research Problem

Business entities are faced with stiff competition due to the rise of technological changes. This has forced the business entities to look for alternative ways to remain competitive. Many business entities have settled on mergers and acquisitions which is expected to be

the only option. According to Kim, (2009), the world has experienced persistent rate of growth in mergers and acquisitions. The latest survey on merger and acquisitions contend that by year 2015, the number of mergers and acquisitions stand over 100million globally (Thomson Reuters).

These forms of business entities are vital because they help businesses achieve synergy from their resources. This however is possible only if it confers some competitive edge to the firms. As a result of mergers and acquisitions the entities achieve various benefits like quick accessibility of technology and products, improved market position and a healthy status financially. In addition, the businesses are able to venture into new geographical market more efficiently, to achieve more growth and expansion since they are able to capitalize on the benefits volume production or economies of scale like reduced costs of operation and increased customer portfolio amongst other reasons (Kemal, 2011).

Straub (2007) argues that mergers are undertaken for economic gains. Among the potential advantages of mergers include combining complementary resources, achieving economies of scale, eliminating inefficiencies and garnering tax advantages. Mergers are mainly performed to improve the company's profits and productivity while significantly reducing the firm's expenses (Heyner, 2007). Mergers have also been noted to result in increased revenues and cost cuts. The need to enhance the market share of institutions in the local banking environment and meet the increasing minimum core capital requirements has prompted firms to engage in mergers. However, merger often fail causing harm the firms, ruining the confidence of their shareholders and tarnishing their credibility in the market share.

In 2008 Viverita explored the effect of mergers and acquisition on six Indonesian commercial banks. The financial performance was compared seven years before and after the merger and the results revealed that the bank's ability to gain profits was increased by the mergers. This was shown by the increase in performance indicators such as ROE and ROA (Viverita, 2008). Jin, 2004 examined the impact of mergers and acquisitions had on the operational aspects of the publicly traded firms in China. Jin conducted a survey of 30 publicly traded firms operating in China.

They used changes in profit margin, revenue, return on assets and total asset turnover ratio before and after the mergers and acquisitions to measure firm performance and undertook tests to ascertain whether M&A resulted to significant changes. The findings revealed that significant improvements were registered in profit margin, total revenue and return on assets following the M&A (Jin, 2004). In 2009 Selvam examined the effect of mergers on the corporate performance of acquirer on selected Indian firms. A sample of 13 firms that had performed mergers in the same industry between the time frame 2002 and 2005 quoted on the Bombay Stock Exchange was undertaken. The aim of the study was to compare the sampled firm's liquidity performance for both the acquirer and target firm before and after the mergers period by use of t-test and ratio analysis. The findings established that the acquirer companies' shareholders increased their liquidity performance after the merger (Selvam, 2009).

Two operational performance studies by Ravenscraft and Scherer (1989), and by Healy et al., (1992) have strongly voiced support for the perceptions about the benefits of acquiring business entities. These authors arrived at different conclusions concerning the benefits of mergers. However, these studies have insufficient data which raises question about whether the findings can be generalized. Scherer and Ravenscraft established noted major declines in profitability of the acquired firms after merger while examining more than 5000 mergers that occurred between the time frame 1950 and 1975, while Palepu, Ruback and Healy noted improvements in profits and sales of both firms after the mergers.

Many mergers and acquisitions have been undertaken in Kenya. The overall objective is aimed at the improvement of the financial health of the firms involved. Many studies have come up with varied results. According to Kioko, (2009) and Nyambura, (2015) the financial performance of the companies greatly improved after mergers and acquisitions. However, Momanyi, (2010) and Odongo, (2012) concluded that financial status of business entities did not have significant change after mergers or acquisitions. This study endeavour to answer the research question; What is the influence of mergers and acquisitions on the financial performance of the firms listed at the Nairobi Securities Exchange?

From the study findings, the researchers have different opinions on the effect of mergers and acquisitions on the financial performance of the business entities. While other findings can confirm a positive impact of the Mergers & Acquisitions, others concluded that mergers and acquisitions had insignificant effect on the financial performance. It is against this background that the present study was undertaken so as to confirm the existing literature.

1.3 Research Objective

The objective of this study was to determine the effect of mergers and acquisitions on the financial performance of companies listed at the Nairobi Securities Exchange.

1.4 Value of the Study

The study findings are of great use in conducting academic research. This will act as empirical reference source, literature for further studies in the area of mergers and acquisition. The study findings will contribute greatly to investment decisions. Investors will make investment decisions on mergers and acquisitions. Investors can make decisions whether to invest in companies that have been formed through mergers and acquisitions by analyzing their financial performances and their profit abilities. The research findings will positively contribute into the finance field in general. Business entities will be able to establish profitability levels. This will in turn help finance managers to get insights and apply the outcome in the risk elimination.

Theoretically, M&A's are often viewed as avenues for exploring knowledge (Vermeulen and Barkema, 2001). This study will provide the platform for tapping into and harnessing the knowledge that resides in mergers and acquisitions. Most studies have focused on obtaining knowledge about either a specific country or a market, or capabilities in technology and innovation through explorative M&As. The mergers and acquisition experience has in a nutshell provided some knowledge that offers an interesting avenue for exploration.

Empirically, this study seeks to understand the association between M&A and financial performance. Furthermore, the study critically analyzed the interaction between target firms and the acquiring firms experience and how it impacts on value creation. Moreover, this study will contribute to organizational learning by seeking to understand whether there is an effect on obtaining access to knowledge without direct experience; That is how does engaging in M&A influence the financial performance of firms entering into such undertakings?

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This section covers the theories and empirical reviews relating to mergers and acquisitions, metrics of financial performance and the literature review summary.

2.2 Theoretical Review

The following theories relate to mergers and acquisitions; Monopoly Power Theory (Lambert, 2001) which implies that mergers and acquisitions are undertaken to realize monopoly power. Empires building theory propounded by Marris, (1963), holds that mergers are planned and undertaken by corporate leaders who desire to optimize their own utility rather than the value of shareholders. Valuation theory or approach states that mergers are planned and executed by managers who are privy to more superior information about the value of the target firm compared to the stock market (Holderness Ravenscraft and Scherer, 1987; Sheehan, 1985; Steiner, 1975). Financial Efficiency Theory (Roll, 1980) which asserts that mergers and acquisitions create synergy and hubris hypothesis (Brigham, 1980) which concluded that errors of over optimism are normally committed by managers during evaluation of the potential targets.

2.2.1 Monopoly Theory

The monopoly theory perceives mergers and acquisition as being planned and executed so as to attain market power. This mutual forbearance theory was advanced by Edwards (1955). Firms engaging in the consolidation program must benefit financially and operationally and thus the M&A process. According to Mueller (1969) mergers and

acquisitions is a way of attaining monopoly power or the execution of an unfriendly activity. Many firms merge to expand their market share in order to either pay low prices to suppliers or charge higher prices to buyers. Lambert (2001) defines monopoly as taking total control of a situation. Monopoly theory asserts that mergers and acquisitions are basically after taking control of a certain market. Monopoly will result into creased market power. When two or more firms merge, the resultant business entity normally is larger than the previously separate entities. When a firm controls a market it means it is likely to earn more profits because monopoly power can dictate the setting of the selling prices which have a direct effect on profitability hence monopoly leads to improved financial performance.

The monopoly theory avers that mergers are formed as a way of creating monopoly and subsequently increased market power through dominance. This is the proper characterization of conglomerate or horizontal mergers. Market power can be realized either by the deliberate restriction of supply, restricting market entry for potential entrants and cross-subsidizing products (Rodermann, 2004; Trautwein, 1990).

Chatterjee, (1986) states that these gains are known as collusive synergy while Porter (1985) refers to them as competitor interrelationships. Jensen (1984) was critical of the monopoly theory after studying the influence of the formation mergers, free cash flow hypothesis and merger cancellations on stock held by competitors. The theory argues that the stocks owned by competitors are supposed to rise when a merger is announced and drop upon a challenge or cancellation of a merger. Since the stocks held by competitors fail to fall on the two latter events Jensen (1984) therefore rejected the monopoly theory.

2.2.2 Empire-building Theory

According to this theory, mergers are planned and executed by corporate leaders seeking to optimize their own utility rather than the value of the shareholders. (Marris, 1963) stated that cross border mergers are usually similar to efforts by firms to achieve growth beyond their optimal sizes, as a means to optimize managerial power or prestige, or to create empires (Rhoades, 1983; Ravenscraft and Scherer, 1987).

This school of thought emanates from the first study about the separation of ownership and control in the corporate world (Berle and Means, 1933). The principal-agent theory justifies the manager's motives. This theory tries to explain that a business management or, the agent, can advance personal interest or pursue objectives that differ from those of the shareholder known as the principals. Personal goals may either be the aspiration to improve one's reputation, to improve financial rewards or achievement of a long-term legacy referred to as empire building (Trautwein, 1990). Due to the inter-twinned nature of these goals with the size of the firm, managers are driven at times to resort to mergers as a way of growing their businesses so as to realize their personal objectives (Rodermann, 1999), Eisenhardt, (1989) were critical of this theory.

Their argument was that an agency relationship always results when a party delegates work to another; a principal and an agent respectively. The duty of an agent is to promote the best interests of the principal. In advancing these interests, the agent engages in in some activities which may have some consequences. Principal bears all the risks or consequences of the activities of the agent executed in the course of the agency. The principal also must pay the agent whereby agent remuneration is determined by the interests of the principal

in the execution of the agency and achievement of the agency objectives. Any gain or benefit to an agent, in form of a remuneration is a cost to the principal. On his part the efforts of an agent confers benefits to the principal, with an assumption that higher effort is directly related to better results for the principal, and reward to the agent.

2.3.2 Valuation theory

This approach opines that mergers are planned and executed by corporate leaders who possess superior information about the firms targeted for acquisition compared to the stock market (Steiner, 1975; Holderness and Sheehan, 1985; Ravenscraft and Scherer, 1987). This theory is based on the assumptions of capital markets that are not efficient and asymmetrical information. The aim of mergers is to achieve a big margin in stock market and the valuation of the firm that is acquiring due to the possession of so distinct information about the target entity only available to the management of the bidders (Rodermann, 1999).

Bidding managers may have special information concerning potential gains that can result by merging the target businesses with theirs or may have noticed an undervalued firm awaiting to be sold. This hypothesis is in conflict with the efficient capital market. The argument advanced is that EMH requires that all information in public domain be incorporated in the stock price (Ravenscraft & Scherer, 1987). Hence where the bidder possesses private information about the target firm's value he must reveal it in his bid. The value of stock would appreciate in tandem with the newly available information leaving the bidder in a winner's or loser situation. Consequently it is clear that efficient market is not only cognizant of the existence of a target firm whose value may have been understated but, also the opportunity to capitalize on exposed private information (Wensley, 1982).

2.2.4 Hubris Hypothesis

According to the hubris hypothesis, management commits mistakes of over optimism in the evaluation of the target party. This can make them bid more and transfer more than they should (Brigham, 1980). Management can easily overestimate the value for their money. They can also state the cost of their post-merger integration lower than the true position or the controlling a larger business entity. The result is the acquisition of a firm that shareholders are not going to gain from. According to the theory managers may be led by hubris (Roll, 1986) to overvalue whatever they may be purchasing. This is despite the fact that their desire is to optimize the firm's value. This usually occurs in instances of consolidation, when managers lacking sufficient market information alter their understanding of conglomerates against strategic focus or when many bidders compete for the same target firm.

Corporate leaders are also likely to underestimate the cost of integration after a merger announcement or overestimate their capacity to control a larger firm. In this instance therefore an undertaking likely to benefit the acquirer is potentially a poor decision strategically where advantages are overstated or costs are understated. This leads to losses to shareholders of the acquiring firm since the market must react to the mistake of the managers. Thaler, (2000) criticized this theory and argued that from the behavioral, economic literature human beings are not good at optimizing anything. More realistic assumptions to govern economic theories accordingly need to be developed.

2.2.5 Financial Efficiency Theory

The idea behind mergers and acquisitions is that they occur because they generate synergy (Roll, 1986). Synergy is the economies form the consideration of business entities where the financial performance of the combined business entities is greater than the individual separate business entities. Normally before any merger or acquisition agreement is reached, the managers of the business entities should evaluate the outcome to determine if it will be beneficial or not. Therefore, mergers and acquisitions will take place if they can generate enough synergies. According to the financial efficiency theory, the optimal return is that with positive value creation. Banerjee and Eckard (1998) and Klein (2001) evidence this suggestion.

Chatterjee (1986), criticized this theory. He averred that when talking about value creation in merger one should be able to distinguish between operative synergies or efficiency gains obtained from economies of scale and scope and allocate these synergies resulting from increased market power and an increased capacity to gain consumer surplus. According to Houston et al., (2001) operating synergies are the most prominent source of gains.

2.3 Determinants of Financial Performance of Companies at NSE

When business firms undergo corporate reconstruction, it is expected that their financial performance will change. According to Campbell, (2001) financial performance measures show how firms have employed asset to generate incomes. It is normally over specified period of time. It can be monthly, quarterly, semi-annually or annually. The determinants include Macroeconomic factors, leverage, company size and liquidity.

2.3.1 Liquidity

This is the extent of buying or selling securities and not affecting the price of the asset (Desai, 1980). It is measured using acid test ratio and current ratio. Current ratio tells us about those assets that can be liquid within 1 year and the liabilities that will be due for payment. Acid test ratio on the other hand is about the availability of sufficient resources which are more liquid to cater for the current liabilities. Business entities with more liquid assets normally outperform the companies with less liquid assets because cash is readily available to cater for their needs at any point in time.

2.3.2 Macroeconomic Factors

Macroeconomic factors include inflation, political instability, fluctuations of the rates of exchange and changes in cost of funds. Political instability like wars will impact negatively on the financial behavior because investments will be slow due to wars. Investors will reduce investment activities for fear of destruction. During wars, client level will reduce and this will in turn affect the financial performance on the other hand political stability will encourage investment hence business entities will be willing to invest more. This will increase the returns and financial performance will definitely improve. Inflation will affect the financial performance of the business entities due to the persistent rise in the prices of the products (Cornell, 2001).

2.3.3 Leverage

Leverage is the amount of debt financing (Wood, 1950), Many companies have resorted to debt financing due to its advantages. However, there are risks associated with debt financing for example the finance charge which is the interest rate. The capital structure of many business entities consist of debt and equity. High amount of debt causes financial distress. Financial distress is a situation where companies face cash flow problems. However, there are benefits associated with leverage. Business entities will always have enough stock to run their businesses because some business entities require the amount of stock which cannot be solely provided by the owner hence need for borrowing. Good debt management skills can have a positive influence on the financial performance.

2.3.4 Company Size

The size of the firm plays an important part in its financial status of a firm and profitability. It is believed that the larger the company the better the financial performance because of the economies of scale. Large companies can easily carryout diversification too which is aimed at reduction of risk. Large companies are able to buy in bulk, by buying in bulk they can be able to enjoy trade discounts hence save on costs. Companies that minimize their costs tend to have higher returns in the long run. Smaller companies on the other hand are constrained due to cash-flow problems hence financial behavior positively co relates to the business size.

2.3.5 Free Cash Flow

According to Roll (1986) Free cash flow is the cash that is produced by a company after undertaking its operation, less the costs of expenditures on assets. It is the cash that is left over after a company pays for its operations and for capital expenditures. As the company can undertake positive Free Cash Flow value shows that the company is left with excess cash while a negative free cash flow shows that the company is left in deficit. The two positions are interpreted differently by different investors depending on their inclinations towards preference of cash dividends over stock capital gains.

Free cash flow is used by the firms to distribute to the shareholders in form of dividends. Therefore, for investors who prefer cash dividends, positive free cash flow is preferred. On the other hand, some investors view positive free cash flows as the incompetence in the management who fail to identify enough projects that they can invest their free cash flows in, so as to earn even higher returns. These kind of investors prefer negative free cash flow as it shows that the company has exhausted all the possible investments that can be undertaken by the company.

2.4 Empirical Review

Empirical literature reviewed presents conflicting outcomes with respect to business entities involved. Some existing empirical literature have proven companies that have resorted to mergers and acquisitions have enjoyed the financial gains. However, other empirical works have revealed no financial gains from mergers and acquisitions of the business entities involved. Maina, (2016) did a study on the influence of mergers and

acquisitions on the financial status of oil firms in Kenya. Using a sample of 13 oil firms randomly selected. The period under study was from 2008 to 2013. The population of interest was 27 oil firms in Kenya. Secondary data extracted from financial statements was used for analysis. The study employed a linear regression model in the analysis. Return on equity and dividend per share were determined 3 years before mergers and acquisitions and 3 years after the undertakings. From the Study findings he concluded that oil firms performed better after merging and acquisitions.

Thomson, (2010) did a study on share price reaction to acquisition announcement in N Y S E. The study aimed to find out the influence of acquisitions on shares value reaction of the entities quoted at the market. A sample of 102 firms was selected from the 200 businesses quoted at the market. Secondary data was used and their findings revealed that stock prices experienced an upward trend a few days prior to acquisitions announcement.

Mohamed et al., (2011) did a study on the influence of mergers and acquisitions on the financial situation of companies in India from 2001 to 2008. 182 firms trading at the Bombay securities market were selected. However, due to time and resource constraints 91 firms were selected as a sample for the study. Linear regression model was used for analysis. Secondary data for companies for analysis was used. Dividend per share and earnings per share was determined over a four years period prior and a similar period after the merger and acquisition. From the findings, the financial performance of those companies improved after mergers and acquisitions.

Jamal & Malik, (2013) did a study about the influence of consolidations on the financial performance of Pakistan banks between 2005 and 2011. All the 157 listed commercial banks were selected for the study. However, 70 banks which had undergone mergers and acquisitions were selected as a sample for study. Data from the published audited accounts from the banks was used. Linear regression model was used in the analysis. Dividend per share and return on assets were determined three years prior merging and acquisition and three years post merging or acquisition. From their findings, these forms of business undertakings had insignificant influence on the financial behavior of the commercial of Pakistani banks.

Vasicek & Stoll, (1998) sought to determine the influence of mergers and acquisitions on the financial behavior of United Kingdom's top 600 firms from 1990 to 1996. 30 mergers and 82 acquisitions were selected for the study. Secondary data was used to analyze return on equity and dividend per share after and before mergers and acquisitions. From their findings, they concluded that financial performance of the United Kingdom firms improved after mergers and acquisitions.

Busse, (2008) did a study to determine the effect of merging and acquiring firms on the financial behavior of Canadian commercial banks in from 2001 to 2006. 102 commercial banks which had undergone merging and acquisitions constituted the study sample of 30 commercial banks. Linear regression model was also employed in the study. He used secondary data to determine the commercial banks' performance measurement indicators which included returns on assets, returns on equity, and dividend per share were determined 2 years before mergers and 2years after mergers and acquisitions. From their findings the commercial banks underperformed after merging and acquisitions.

Osoro, (2010) did a study on the impact of merging and acquisition of firms on the financial situation of insurance firms in Kenya between 2001 to 2007. A sample of 6 mergers and 8 acquisitions was selected for the study from the 21 mergers and acquisitions. Secondary data extracted from the financial statements of the insurance companies in Kenya was used. Earnings per share and dividend per share were determined and computed 2years before mergers and acquisitions and from the findings of the study, insurance firms underperformed after mergers and acquisitions.

Rono, (2012) did a study on how merging and acquisitions of construction and manufacturing companies influenced their financial position in Kenya between 2003 & 2010. The population of interest was 13 construction and manufacturing companies which had undergone mergers and acquisitions. A sample of 7 construction and manufacturing companies was selected for analysis. Linear regression model was employed in the analysis. Key indicators like return on assets and return on equity were computed and compared. She concluded that financial behavior of construction and manufacturing companies improved after mergers and acquisitions.

Odongo, (2014) did a study on how merging and acquisitions influenced the financial performance of the commercial banks trading in the NSE in Kenya between 2008 and 2012. A sample of 10 commercial banks which had undergone mergers and acquisitions were selected for the study. Secondary data from published financial statements of the commercial banks in Kenya was used. Data was analyzed two years before mergers and acquisitions and two years after mergers and acquisitions. Financial performance

measurement indicators which included returns on assets and return on equity were determined for comparison. The study also employed the regression model to study the relationship among the study variables, from her findings mergers and acquisitions had insignificant effect.

Kauki, (2011) did a study on the effect of mergers on the financial performance of commercial banks trading at the NSE from 2006 to 2010 in Kenya. A sample of 8 commercial banks which had undergone mergers was selected. Secondary data from the published financial statements of the commercial banks in Kenya was used. Data was analyzed three years after mergers and three years before mergers. Financial performance measurement ratios which included dividend per share and earnings per share were computed and compared. The study also employed the linear regression model in the analysis. From his findings, the financial performance of commercial banks greatly improved after mergers.

Kimeu, (2015) sought to understand how merging of firms influences the financial behavior of the oil marketing firms in Kenya between 2008 to 2013. A sample of 10 oil marketing firms was selected for the study. Secondary data extracted from their financial statements was used. Financial performance was measured by return on assets, return on equity and dividend per share for the oil marketing firms. Linear regression model was used for analysis. From the study findings, the oil marketing firms underperformed after mergers.

From the study findings, the researchers have different opinions on the influence of merging and acquisitions on the financial performance of the business entities. While other findings can confirm a positive impact of the Mergers & Acquisitions, others concluded that mergers and acquisitions had insignificant effect on the financial performance. It is against this background that the present study will be undertaken so as to confirm the existing literature.

2.5 Conceptual Framework

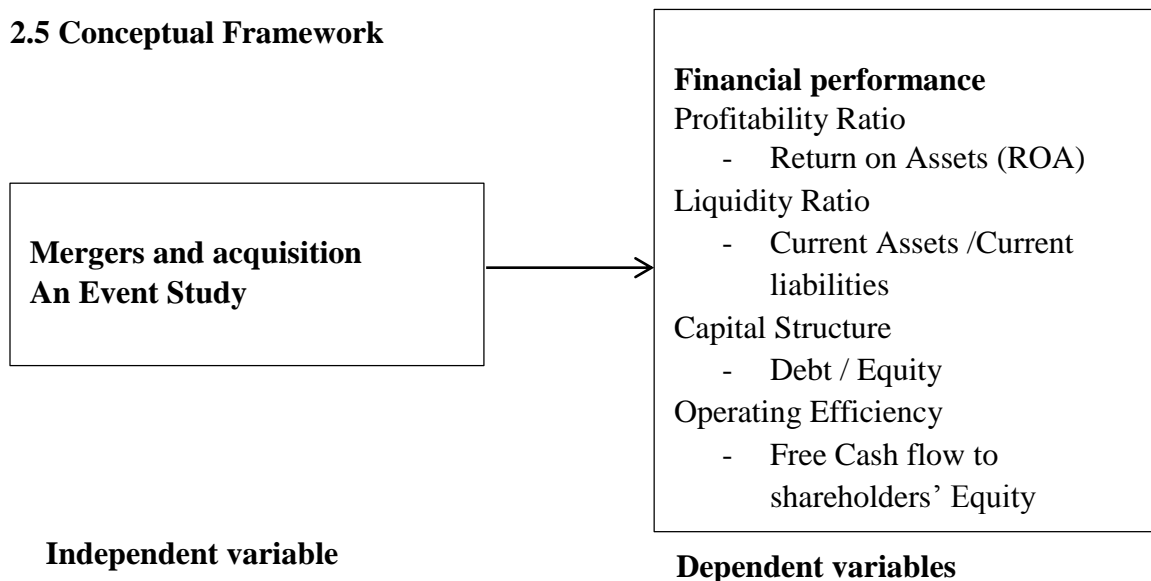


Figure 2.1: Conceptual Framework

The figure above shows the relationship between the independent variable which is an event study of mergers and acquisition and how this event affected financial performance of companies listed at NSE.

2.6 Summary of Literature Review

This constitutes the theories used were discussed and included; monopoly theory, empire-building theory, valuation theory, hubris hypothesis and financial efficiency theory. The determinants of financial performance which included; liquidity, macroeconomic factors, leverage, company size, free cash flow to equity ratio and the empirical review which included Omollo (2015), Maina (2016), Kauki (2010), Mohamed et al. (2011), Jamal and Malik (2013), Vasicek and Stoll (1998), Busse (2008), Osoro (2010), Rono (2012), Odongo (2014) and Kimeu (2015) which had presented varied outcomes on the results on the effect of mergers and acquisition. Majorly, studies have been conducted on segment basis. The current study was therefore conducted in all the segments of the listed companies.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introductions

The section brings out the methodologies used to carry out the research. The research design applied, the population, data collection method and the methods of analyzing data.

3.2 Research Design

This is the methodology employed in the research process (Mugenda, 2005). The study used a descriptive research design.

3.3 Population of the Study

A Population is a well-defined set of elements subject to the investigation (Mugenda, 2005). In this study the population is composed of all companies listed at NSE and that had undergone mergers and acquisitions between the years 1997 to 2017. A total of 18 companies were identified, out of which 15 had all the information needed for analysis.

3.4 Data Collection

Secondary Data from the companies' published financial statements was obtained from their websites and NSE handbook for three years after and three years before merger for the companies. Data collected include; total assets, total liabilities, total debt, total equity, current assets, current liabilities and profitability after tax for three years, after and three years before merger for the companies.

3.5 Data Analysis

Data analysis is the act of processing data to make it useful. Data was analyzed 3 years prior to merging or acquisition and 3 years after, so as to assess whether merging or an acquisition will have some substantial influence on the financial performance of the firms. To establish some relationship among the different variables in the study, a test at 5% significance level was conducted on the mean of Profitability ratio, Liquidity ratio, Capital structure ratio and Cash Flow Ratio. The mean and standard deviations before and after the mergers and acquisitions was computed and comparisons made and the t-value for independent sample means determined that showed whether the means of the two populations are significantly different to show any effect of merger on financial performance.

The equation that compares the variables on financial performance is defined as:

$f(\text{Profitability ratio, Liquidity ratio, Capital structure ratio, Cash flow Ratio}) = f(\text{merger})$

$f(Y_1, Y_2, Y_3, Y_4) = \text{Merger}$

Profitability ratio (Y_1) is measured by the return on Assets

Liquidity ratio (Y_2) measured by current assets to current liabilities ratio

Capital Structure ratio (Y_3) measured by total debt to shareholder's equity ratio

And Cash-flow ratio (Y_4) measured by total free cash flows to total equity.

3.6 Diagnostic Tests

Every model makes various assumptions that must be met so as to efficiently use the model in making statistical inferences. The independent test statistic for sample means uses statistical t tests that also undertakes various assumptions about the data. The model makes

the assumption that data follows a normal curve. This means that a normality diagnostic test is undertaken. Normality test is undertaken by the use of skewness and kurtosis that determines whether data is positively or negatively skewed. It also shows whether data is flat or sharply distributed.

The statistical test also undertakes an assumption on the variability of the sample means. This means that the variances between the means of the two populations are similar. In order to undertake a diagnostic test on this, Levene's test on equality of variances was undertaken. If data fails, this test then a different row is generated that is used to show the statistical value for the situation when the means are not similar.

3.7 Test of Significance

The test study undertaken is a two tailed test. This is because the null hypothesis assumes that the means of the financial performance of the companies before M&A is equal to the means of the financial performance of these companies after M&A. It therefore implies that the difference in sample means for financial performance may either be higher after merger and acquisition or lower.

The test of significance for a two tailed test of independent sample mean therefore is undertaken by comparing the confidence level (alpha value) which was set at 5% and the calculated value of significance (p value). A p value that is greater than the alpha value means that the test has failed to reject the null hypothesis and the vice versa.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction

In order to determine the effects of mergers and acquisitions on financial performance of companies listed at the NSE, then statistically independent sample mean analysis was undertaken that emphasized on obtaining the mean of the financial performance that was measured by returns on assets, current ratio, debt/equity ratio and free cash flow to equity ratio for the companies listed at NSE and had undergone merger or acquisition. Data collected three years before the M&A was considered and compared to similar data undertaken three years after the M&A. Various tests were also undertaken on the data collected in order to understand the variables well. The analysis is well stipulated on this chapter by use of tables and discussions. A discussion of research findings was also undertaken.

4.2 Response Rate

Secondary data was collected on all the firms listed at the NSE and which had either merged or acquired other companies. Their financial performance data was obtained which was determined by the ratio of profitability, liquidity ratio, equity to debt ratio and free cash flow to equity ratio of the firm for 3 years before merger and three years after merger. There were a total of 15 firms that were identified as having merged or been acquired by other companies within the years 1997 to 2017. The 15 firms had all the information three years before merger and three years after merger. Some companies such as the acquisition

of Chase bank by Kenya Commercial Bank, did not have three years of information after data. From a possible of 18 companies, 15 companies were found to have all the required information for analysis. This represented 83% response rate which according to Mugenda & Mugenda (2003) a response rate of more than 60% is considered appropriate for data analysis.

4.3 Diagnostic Test

Normality tests and Levene's test on variability were conducted accordingly. Normality test was conducted in order to ensure that the data followed characteristics of a normal curve. This test included test of skewness which measures the leaning of data distribution either on the right or on the left. Data that has normal curve distribution of data tendencies is devoid of high positive or negative value of skewness. Kurtosis on the other hand is explained by the flatness or the sharpness of data. High kurtosis means that the data is sharp with a low value showing flatter data distribution. A standard practice suggests that a value that is greater than +3 or -3, for both kurtosis and skewness suggests that data is not normally distributed. The variable is therefore standardized for the purpose of analysis.

Table 4.1: Normality Test Table

	Skewness		Kurtosis	
	Statistic	Std. Error	Statistic	Std. Error
ROA	3.022	.254	9.940	.503
Current Ratio	4.225	.254	21.052	.503
Debt-Equity Ratio	1.050	.254	.193	.503
Free cash flow to equity	1.557	.254	1.988	.503
Valid N (listwise)				

Source: Author,
2018

The variables representing financial performance measured by profitability (ROA ratio), and liquidity (measured by current ratio) had both skewness and kurtosis of greater than +3. It therefore showed that the two data variables did not have a normal curve distribution. The two variables were therefore standardized (normalized) for further analysis. Capital structure ratio and free cash flow to equity ratio had kurtosis value within the acceptable range of +3 and -3 and were therefore construed to have normal curve characteristics. Levene's test on equality of variances on the other hand is used to show that the population of each variable before merger has equal variance with the population of the variable after merger. This is explained on table 4.3

4.4 Descriptive Statistics

Descriptive statistics describes the data collected for each variable. It describes in form of the maximum value, the minimum, standard deviation of the data and variance of each population of data as shown in table 4.2 below.

Table 4.2: Descriptive Statistics

	Years After Merger	N	Mean	Std. Deviation	Std. Error Mean
Zscore: ROA	>= 0	45	.1790030	1.23176757	.18362107
	< 0	45	-.1790030	.66327617	.09887537
Zscore: Current Ratio	>= 0	45	.1252488	.98672751	.14709265
	< 0	45	-.1252488	1.00846839	.15033359
Zscore: Debt-Equity Ratio	>= 0	45	2.858863	3.3454347	.4987080
	< 0	45	3.216858	3.4146838	.5090310
Zscore: Free cash flow to equity	>= 0	45	.745408	.9247187	.1378489
	< 0	45	.657951	1.1002013	.1640083

Source: Author, 2018

The financial performance was measured by return on total assets, liquidity, debt and free cash flows. Return on assets shows how the management is able to utilize its assets in generating profits for the company. This variable was standardized and the table shows the values for each variable after merger (days after merger ≥ 0) and before merger (days after merger < 0). The normalized ROA after merger had a mean of 17.9% and a standard deviation of 123.2%. The mean of ROA before merger was a loss of 17.9% with 66.33% deviation. From looking only at the mean of both of these populations, it would therefore follow that ROA after merger was better than ROA before merger.

The liquidity level of the company was measured by the ratio of current assets to current liabilities. The variable was also standardized and the distribution violated the terms of a normal curve. The mean for liquidity after merger was .125 with a standard deviation of .987 while the mean for pre - merger was -.125 with a standard deviation of 1.008. This shows again that liquidity for the companies was better after merger than it was before merger.

The Capital structure was measured by debt financing to equity financing. It shows the extent the company relied on debt financing as compared to equity financing. After merger the mean for capital structure was 2.86 with a standard deviation of 3.35 while the capital structure before merger had a mean of 3.22 and a standard deviation of 3.41. This shows that the companies relied more on debt before merger than they did after the merger and acquisition.

Free Cash Flow to shareholder's equity measures the available free cash flow for each unit worth of share for equity shareholders. It is the excess cash flow after the company finances its operations and makes prepayments, and meets its financial obligations. After merger, the mean for free cash flow to equity ratio was .745 with a standard deviation of .925 while before merger the ratio was .66 with a standard deviation of 1.1. This again showed that the companies had excess cash flow after merger than the excess cash flow they had before merger.

4.5 Independent T test for Sample Means

4.5.1 Introduction

The independent T test for sample means is also called two sample t-test. The tests is used to determine whether there exist statistically significant differences between means of two unrelated groups. In this case the study is used to determine whether the mean of various variables before merger was statistically different from the means of these variables after merger and acquisition.

4.5.2 Performing Student t-test.

In order to undertake a statistical student t test which in this case is the independent t test statistical for sample means, we define the process that needs to be followed. The first instance is to define the null hypothesis. The null hypothesis in this study states that the mean of financial performance for companies listed at NSE before merger is the same as the mean of financial performance of the companies after merger. The alternative hypothesis is the direct opposite which states that the two means of the two populations are not equal. The test statistic is therefore a two tailed test since there is no emphasis on direction needed.

For a two tailed tests, the decision criteria that is applied in order to decide whether to accept or reject the null hypothesis is comparing the alpha which is set at 5% significance level with the p value or the calculated value of significance of the study. If the p value is greater than the alpha value, then the study fails to reject the null hypothesis and assumes that the means for both populations are equal. If the alpha value is greater than the significance value, then the null hypothesis is rejected which means that the two populations means are not equal and since we know that the mean after merger is greater than the mean before merger. We conclude that the difference is statistically significant.

4.6 Independent T test Statistic

One of the major assumption that is made by the independent t test for sample means is similarity in variances. The test assumes that the two population have similar variances. The variability test is undertaken by use of Levene's test for equality of variances. In the table 4.3 the Levene's test for equality of variances show a significance value (p value) of 0.09 for ROA which is higher than the alpha value of 0.05. We therefore conclude that the variances of the two populations are not equal for ROA.

In order to determine whether the difference in the population means is significant or not, we first determine the null hypothesis and the decision rule to reject or fail to reject the null hypothesis. The null hypothesis states that there is no difference between the means of the financial performance of the companies before merger and after merger. All analysis are undertaken in 95% confidence level which provides a significant level of 5%. The student t test statistic undertaken is a two tailed test as no order or any direction in testing the data.

To undertake the t-test equality of means we will use the row where equal variances of

Table 4.3 Independent Samples Test

		Levene's Test for		t-test for Equality of Means						
		Equality of		t	df	Sig. (2-	Mean	Std. Error	95% Confidence	
		Variances							tailed)	Difference
		F	Sig.						Lower	Upper
Zscore:	EVA	5.878	.017	1.717	88	.090	.358	.209	-.056	.772
ROA	EVNA			1.717	67.54	.091	.358	.209	-.058	.774
Zscore:	EVA	3.827	.054	1.191	88	.237	.250	.210	-.167	.668
Current Ratio	EVNA			1.191	87.96	.237	.250	.210	-.167	.668
Zscore:	EVA	.531	.468	-.502	88	.617	-.358	.713	-1.77	1.058
Debt/Equity	EVNA			-.502	87.96	.617	-.358	.713	-1.77	1.058
Zscore:	EVA	.158	.692	.408	88	.684	.087	.214	-.338	.513
FCF/Equity	EVNA			.408	85.47	.684	.087	.214	-.338	.513

means is not assumed denoted as EVNA (equal variances not assumed), in the table. The

significance level (p value) for a two tailed test is 0.091 which is greater than the alpha value of 0.05. This means that the study fails to reject the null hypothesis. It is therefore concluded that the difference in means of financial performance of companies listed at NSE before merger and after merger are not statistically significant.

4.6.1 Control Variables

The control variables in the study were made up of current ratio to measure liquidity, capital structure measured by debt to equity ratio and free cash flow to share holders' equity ratio. The t test statistics for these control variables are also shown in the table 4.3 in which case similar process as that used in determining whether the mean of profitability ratio before merger was similar to the mean after merger is also used for each variable.

The significance for current ratio was .237 which is also greater than alpha of 0.05. We therefore fail to reject the null hypothesis by suggesting that there is no difference in means of liquidity levels for the firms before and after merger. Similar results are also for capital structure and for free cash flow to equity ratio as they all have their p values greater than the alpha value of 0.05. We therefore conclude that there is no statistically significant effect of mergers and acquisitions on either profitability, liquidity, capital structure or free cash flow to equity ratio for firms listed at NSE.

4.7 Discussion of Findings

There were 18 companies listed at the NSE that had announced mergers and acquisitions within the study period of 1997 and 2017. However, three of these companies did not have all the information required as the study targeted data three years before merger and three years after merger. The data obtained from the 15 companies therefore represented a response rate of 83% which was considered sufficient as a basis of deriving conclusions from this study.

The analysis of the data used an independent t test statistic for sample means in determining whether the mean of the population of financial performance of these companies before merger and after merger had statistical significant differences or not. This analysis however makes various assumptions in which diagnostic tests were undertaken to confirm whether the collected data conformed to these assumptions or not.

The test assumes that data follows tendencies of normal curve and therefore a normality test was undertaken by the use of kurtosis and skewness. The results showed that all the variables had kurtosis and skewness in the range of +3 and -3 except for Return on Assets and Current ratio that did not show normal curve distribution characteristics as they failed both kurtosis and skewness test. The data was therefore standardized in order to normalize it for the two variables. The other two variables were okay.

The other assumption made by this test is that population before merger and population after merger for each variable had equal variances. This was tested by the use of Levene's test of equal variances. The p value for all the variables was greater than alpha and therefore the study assumed that the variances of the populations before and after merger for all the variables was not equal. The study therefore conducted a t-test for equality of means when equal variances is not assumed (EVNA).

The mean of profitability before M&A was found to be 6.3% while the mean after merger and acquisition was found to be 13.15%. It is clear that the mean after M&A is higher and almost double the mean before M&A. However, a t test statistic had to be undertaken in order to show whether the difference was statistically significant or not. The student t test however failed to reject the null hypothesis as p value was greater than alpha value. The study therefore concluded that the difference in means before and after M&A was not statistically significant.

Similarly, liquidity level was compared after merger and before merger. The standardized score for liquidity after merger was 1.25 and before merger was -.125. It was therefore evident that liquidity after merger was higher than before merger. However, the independent sample test statistic showed a p value (.237) that was greater than alpha value of .05. The conclusion was that the difference in means after merger and before merger was not statistically significant.

The mean for capital structure (Debt/equity) level was determined and the mean for this ratio after merger was less than the ratio before merger 2.86 and 3.22 respectively. It showed that more companies after merger were able to access debt and thus increased their debt to equity financing, than the companies before merger. This difference in means was also not statistically significant with p value of .617 which is greater than alpha value.

Finally, free cash flow to equity ratio after merger was greater than free cash flow before merger at .745 and .658 respectively. This shows that there was more free cash flow available to the shareholders after merger than it was before merger. However, the t statistic showed a p value of greater than 0.5 of which the study concluded that there was no significant effect of mergers and acquisitions on free cash flow.

Table 4.4: Summary of Results and Findings

Variable	Mean results before Merger	Mean Results after Merger	Significance
Financial Performance	Lower	Higher	Not significant
Liquidity	Lower	Higher	Not significant
Debt/Equity ratio	Higher	Lower	Not significant
Free cash flow to equity ratio	Lower	Higher	Not significant

Source: Author, 2018.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

In this chapter the study findings are well summarized and compared to empirical findings of similar studies. Theories that are emphasized or provisions of the theory critiqued are also highlighted. Conclusions are then drawn from these findings and recommendations based on the conclusions are made. The limitations of the study and areas to be undertaken further research are also highlighted in the chapter.

5.2 Summary of Findings

The study aimed to look at the effects of mergers and acquisitions on the financial performance of companies listed at Nairobi Securities Exchange. A total of 15 companies listed at NSE had information available three years before M&A and 3 years after M&A. Financial performance was measured using returns on assets ratio, current ratio, debt to equity ratio and free cash flow to equity ratio. The model of analysis used was independent sample mean test that tried to compare the means of each variable before merger and after. The study aimed to seek whether the null hypothesis would be rejected for each variable that would confirm that the differences between the returns on assets ratio, current ratio, debt to equity ratio and free cash flow to equity ratio of the companies before and after merger is statistically significant.

Diagnostic tests were undertaken in order to determine whether data complied with the assumptions of the model. These tests were test for normality and Levene's test for equal variances. The data failed in both of these tests and transformations had to be done to the data and the manner of undertaking the t-statistic so as to have error proof findings.

The alpha value was compared to the p value of t test statistic of means. The P value was greater than the alpha value for all the variables. Financial performance measured using Profitability (return on assets ratio) compared $0.091 > 0.05$, Liquidity (Current assets /current liabilities ratio) compared $0.237 > 0.05$, Capital structure (Debt/Equity ratio) compared $0.617 > 0.05$ and free cash flow to equity ratio compared the value $0.684 > 0.05$. Since the study was a two tailed test, only the test of significance was required to reject or fail to reject the null hypothesis.

The study therefore failed to reject the null hypothesis for all the variables, which means that the means before merger and after merger of profitability, liquidity, capital structure and free cash flow ratio were not significantly different from each other. These findings therefore led to the conclusion that despite that the actual mean of profitability after merger was more than double the mean of profitability before merger, the performance of companies before merger is similar to the performance of the same companies after merger. Similarly, the performance of the companies before merger and after merger on liquidity, capital structure and free cash flow ratio were statistically similar.

The study therefore showed that there is no statistical significant effect of mergers and acquisitions on financial performance of companies listed at the NSE. This study agrees with empirical studies that were undertaken by Jamal & Malik (2013) and Odongo (2014). Jamal & Malik (2013) their study effect of financial performance of M&A on commercial banks in Pakistan found out that M&A had insignificant effect on financial performance of commercial banks in Pakistan. Odongo (2014) also found out that mergers and acquisitions had insignificant effect on commercial banks listed at NSE.

On the other hand, this study contradicts empirical studies that had been previously undertaken. Maina (2016) found that oil firms in Kenya performed better after mergers and acquisitions. Thomson (2010) on the other hand also found that the stock prices increased days before mergers and acquisitions took place. Busse (2008) found that commercial banks underperformed after M&A.

5.3 Conclusion

The study concludes that despite slight increases on financial performance for the companies after merger and acquisitions such increases are not statistically significant. This means that companies do not improve their financial performance by engaging in M&A. More synergy and approach is needed to enhance financial performance of these firms listed at NSE. The financial performance was measured by profitability, liquidity position, capital structure and free cash flows. Profitability (ROA) measures the profits that is generated by each shilling worth of assets invested by the company. The total profits might increase after M&A but so does the total number of assets. However how much the company management is able to utilize the assets efficiently to generate more profits is the right measure of increase in profitability used to measure financial performance.

The study concludes that undertaking a merger and acquisition decision should not be pegged on improving the financial performance of the company's profitability, liquidity position, capital structure or free cash flow. This is because the effect of merger and acquisition on these variables is not statistically significant. The study also concludes that mergers and acquisitions do not increase financial performance but rather other factors influences financial performance. The increase in financial profits of merged companies would not necessarily mean that there is increase in financial performance. This is due to the fact that financial performance would be controlled by the number of assets and how these assets are utilized to generate enough profits to enable the company experience financial performance.

5.4 Recommendations

The results of this study showed that investors and shareholders should not assume that when companies merge and acquire other companies will automatically lead to increased financial performance measured using profitability, liquidity, capital structure and free cash flows. The study therefore recommends managers and investors to undertake due diligence when making decisions to merge or acquire as it is not automatic that the merger or the acquisition will lead to improvement in financial performance. This study proves that mergers and acquisitions have no impact on financial performance of companies listed at NSE.

The study would also recommend to the policy makers and regulatory authority to make provisions that would require companies engaging in either mergers or acquisitions to ensure that they set performance limits that would enhance financial performance of these companies after mergers and acquisitions. Most mergers and acquisitions that take place in Kenya are motivated by meeting the minimum requirements set by the regulating authority. These requirements include minimum capital adequacy ratio, minimum asset base among others. If similar interests would be focused on financial performance measures, then mergers and acquisitions would lead more to improving financial performance of these companies.

5.5 Limitations of the Study

The study looked at 3 years before and after M&A. We would expect different results if the period of study was extended to cover a longer period both before and after M&A due to business performance fluctuations overtime which has a direct impact on financial performance. The study therefore was limited by the period of study that was used in order to determine the effect of mergers and acquisitions on financial performance of firms listed at NSE.

The study used secondary data that was collected from these companies' websites, NSE handbooks and CMA manuals. It was difficult obtaining information on mergers that happened in the 1990s as most of these companies after merger ceased to be operational and their records is only available in limited formats and limited sites. The older the required data, the harder it is to access the information. The researcher could also not authenticate the validity of the data, as most of the published financial statements in the websites are unaudited financial statements.

The study also used 15 companies in a capital market that is composed of 64 companies that have been listed at the NSE. The number is relatively small to be used in generalizing the results to be used for the entire market. Most of the mergers and acquisitions were also obtained from the banking sector, which shows that some important sectors such as agricultural sector did not have any representative company.

The study obtained data of 3 years' financial performance of companies before and after merger. The data however was of different years that had experienced different situations of inflation, economic growth stability, exchange rate fluctuations among others. This study did very little in ensuring that the effect of changes in these variables have been factored in, on the data collected.

5.6 Suggestions for Further Studies.

This study focused on companies listed at the NSE. This limited the number of companies to be studied. A similar study could further be undertaken by future researchers looking at all mergers and acquisitions that have taken place in Kenya. The study might also consider increasing the years of study, after and before the said merger and acquisition to ascertain if different results can be achieved. A further study should perhaps be undertaken on effect of M&A on financial performance and control the financial performance for each merger with macroeconomic factors such as interest rates, inflation rates, and economic growth among others. The study would obtain a more accurate result as inflation rates keep on fluctuating from time to time. Data obtained in the 1990s should be well adjusted for inflation and other macroeconomic factors before it is compared with recent data.

A similar study could further be undertaken by future researchers as per segment basis of the companies listed at NSE to find out whether the results are consistent across all sectors of the economy. It would be more appealing to find out whether in some sectors financial performance of companies improved after M&A. On the other hand, further study can be done on companies listed at NSE but using different variables to measure the financial performance of the listed companies both before and after mergers and acquisitions.

This study only dealt with firms listed at NSE. Further study should be carried out to determine the effect of mergers and acquisitions on financial performance of unlisted firms. This will be interesting to find out whether the financial performance of companies listed at NSE could have been manipulated to mislead the market of better expected financial performance due to the merger or acquisition. Further study can be done on the effect of mergers and acquisitions on financial performance of companies listed at NSE but not only using secondary data but to combine both primary and secondary data. Primary data can provide useful insights that may not be captured by secondary data. It could be that the change in financial performance as a result of mergers and acquisitions is as a result of merger or acquisition altogether with other measures employed concurrently with the merger or acquisition.

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APPENDICES

Appendix I: Companies at the NSE that have merged between 1997 and 2017

<u>INSTITUTION</u>	<u>MERGED WITH</u>	<u>CURRENT NAME</u>	<u>DATE APPROVED</u>
NIC BANK LTD	AFRICAN MERCANTILE	NIC BANK	1997
BARCLAYS BANK OF KENYA	BARCLAYS MERCHANT FINANCE LTD	BARCLAYS BANK OF KENYA	1999
STANDARD CHARTERED LTD	STANDARD CHARTERED FINANCIAL SERVICES	STANDARD CHARTERED BANK LTD	1999
TRUST FINANCE	TRUST BANK LTD	TRUST BANK LTD	1997
COOPERATIVE BANK KENYA LTD	COOPERATIVE MERCHANT BANK	COOPERATIVE BANK KENYA LTD	2002
ACCESS KENYA LTD	DIMENSION DATA	DIMENSION DATA	2013
ECOBANK KENYA LTD	EABS BANK LTD	ECOBANK LTD	2008
OLYMPIA CAPITAL	KENMAR GROUP	KENMAR OLYMPIA GROUP	2012
NBK LTD	KENYA NATIONAL CAPITAL	NBK KENYA LTD	1999
DTB BANK LTD	PREMIER SAVINGS & FINANCE	DTB BANK LTD	1999
TOTAL KENYA LTD	ELF OIL K LTD	TOTAL KENYA LTD	2001
PAN AFRICA GENERAL INSURANCE	APOLLO INSURANCE	PAN AFRICA INSURANCE LTD	2003

CFC BANK LTD.	STANBIC BANK LTD.	CFC STANBIC BANK LTD.	2008
KENYA OIL	KOBIL PETROLEUM LTD	KENOL KOBIL	2008
SAVINGS AND LOAN (K) LIMITED	KENYA COMMERCIAL BANK LIMITED	KENYA COMMERCIAL BANK LIMITED	2010
KCB BANK	CHASE BANK	KCB BANK	2016
I & M BANK	GIRO COMMERCIAL BANK	GIRO COMMERCIAL BANK	2017
DIAMOND TRUST BANK KENYA LTD	HABIB BANK KENYA LTD	DIAMOND TRUST BANK KENYA LTD	2017

Source: Capital Market Authority

Appendix II: Data Collected

Days After Merger	ROA	Current Ratio	Debt-Equity Ratio	Free cash flow to equity
-1	0.00531	2.520312	5.327781	0.340448
-2	0.057721	2.365071	3.195943	0.350107
-3	0.031222	2.09543	6.510917	0.938697
-1	0.166009	1.44	0.085402	0.399829
-2	0.106501	1.26	0.117175	0.488965
-3	0.101262	0.84	0.044892	0.336876
-1	-0.02445	1.735646	0	-0.38623
-2	0.066525	1.646993	0.004898	-0.37667
-3	0.072101	1.525171	0	-0.21996
-1	-0.05689	3.816929	1.724958	0.208829
-2	-0.00508	3.434944	1.60119	0.38244
-3	-0.00839	2.200145	2.291391	0.592715
-1	0.043135	3.580517	0.130335	0.036838
-2	0.044128	4.222259	0.110525	0.077877
-3	0.042637	8.723592	0.460766	0.153752
-1	-0.05144	0.518324	9.033898	2.882897
-2	0.036128	0.539962	6.375162	3.809832
-3	0.034989	0.56744	7.16	4.061538
-1	0.057374	0.512198	10.24945	3.315751
-2	0.074202	0.465106	13.044	2.834148
-3	0.0231	0.818711	7.735526	2.090789
-1	0.04975	0.593252	3.686585	0.102519
-2	0.042223	0.532112	3.383605	0.18865
-3	0.026198	5.520217	3.106047	0.305581
-1	0.020534	0.536724	6.663323	0.283386
-2	0.012448	0.522628	8.341647	0.154147
-3	-0.08259	0.569331	4.546499	0.199164
-1	0.023286	0.451656	6.195722	0.284848
-2	0.010064	0.4415	7.391734	1.175801
-3	0.077539	6.250363	0.066347	1.008668
-1	0.027366	3.616354	0.397903	0.011255
-2	0.032055	3.782456	0.352488	0.019488
-3	0.027615	9.21006	2.724936	0.216265
-1	-0.06724	0.240164	1.469839	0.201704
-2	0.079537	0.245479	1.871953	0.247835

Days After Merger	ROA	Current Ratio	Debt-Equity Ratio	Free cash flow to equity
-3	0.068142	0.250419	1.769635	0.40398
-1	0.263285	0.597423	6.005263	0.440602
-2	0.541219	0.85207	5.250819	0.871644
-3	0.331551	1.12556	5.963042	1.429031
-1	0.021922	0.995037	0.131098	-0.01341
-2	0.017905	1.0055	0.118375	-0.02022
-3	0.016181	1.056245	0.111187	0.078636
-1	0.020619	5.701754	0	0.648276
-2	-0.03901	1	0.006329	-0.98734
-3	0.527473	82	0	0.037801
3	0.048417	2.072714	4.456111	0.614786
2	0.041483	2.017551	5.237082	0.925956
1	0.044206	2.143587	4.656001	0.739036
3	0.107878	0.95	0.047232	0.186223
2	0.133163	1.24	0.049665	1.297521
1	0.149665	11.30	0.057814	0.578804
3	0.051278	1.490204	0.00222	0.187482
2	0.166067	1.277438	0.002986	0.223941
1	0.111267	1.733394	0.004354	0.066839
3	0.030542	1.496081	2.235294	0.187735
2	0.047619	1.343352	2.358754	0.504834
1	0.071152	1.197903	2.004378	0.796848
3	0.032521	39.88187	0.081961	2.245882
2	0.029271	16.10627	0.197912	1.75655
1	0.201013	14.31348	0.149984	3.191104
3	0.032637	0.697788	3.254083	2.132486
2	0.00738	0.580255	4.112264	2.023585
1	0.012132	0.567453	4.630237	1.415301
3	0.023398	0.485773	10.84176	2.672598
2	0.034316	0.511853	9.893763	2.696465
1	0.03571	0.513352	9.996084	2.874333
3	0.043501	5.752432	3.191543	-0.04567
2	0.016008	5.994156	2.850289	0.330025
1	0.075171	5.762786	2.950807	0.624557
3	-0.09664	0.509565	10.88363	-0.00047
2	-0.09207	0.512813	10.1174	0.569374
1	0.012395	0.519763	8.789088	0.374186
3	-0.00686	10.76623	0.037475	0.677502

Days After Merger	ROA	Current Ratio	Debt-Equity Ratio	Free cash flow to equity
2	0.016748	30.29188	0.013005	0.567996
1	0.038384	30.41954	0.012504	0.336803
3	0.03253	51.955	2.542698	-0.09298
2	0.01947	24.88964	2.221148	-0.36611
1	0.002922	25.65442	2.047291	0.614351
3	0.044334	0.22725	1.589196	0.148514
2	-0.013	0.207167	1.547118	0.153971
1	0.02965	0.203493	1.098353	0.149893
3	0.383562	0.592641	5.499383	1.22501
2	0.376812	0.640242	3.979411	0.808183
1	0.370206	0.722818	4.396587	0.993278
3	0.89145	1.199523	0.15102	0.071406
2	0.956942	1.112025	0.1981	0.135208
1	0.869117	1.110047	0.240676	-0.59198
3	0.151163	0.913793	0.007143	0.010714
2	0.184564	5	0.011152	-0.04461
1	0.2	0.475096	0.003891	-0.42412