

**EFFECTS OF MERGERS AND ACQUISITIONS ON FINANCIAL PERFORMANCE
OF OIL COMPANIES IN KENYA**

BY

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DECLARATION

This research project is my original work and has not been presented for examination to any other university.

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

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DEDICATION

This research project is dedicated to my parents Ileri and Mercy for their love and support towards my education and to my wife Irene without whose caring supports it would not have been possible.

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ABSTRACT

A Merger refers to the combination of two or more firms, in which the resulting firm maintains the identity of one of the firms, usually the larger. An acquisition, also known as a takeover or a buyout, is the buying of one company (the 'target') by another. The study set out to find the effects of mergers and acquisition on financial performance of oil industry in Kenya.

This study took on a causal research design. Causal research design is consistent with the study's objective which is to determine the effect of mergers and acquisition on financial performance of oil industry in Kenya which can be measured through long-run profitability, leverage and liquidity. Gay and Airasian (2003) note that causal research designs are used to determine the causal relationship between one variable and another. Population is a well defined set of people services, elements, events, group of things or household that are being investigated. In this study the target population was the oil companies in Kenya with keen interest on those that have gone through mergers and acquisition. The process of data collection involved self administered drop and pick questionnaires distributed to management and employees of the oil industries involved. The use of audited accounts enhanced the data received from respondents. Qualitative analysis was used to analyze the views of respondents on mergers and acquisition. Also Chi-Square test was used to establish the relationship between pre and post merger/acquisition and linear regression model enhanced the analyses of the effects of merger and acquisition on financial performance.

According to the findings, majority of these companies were established through mergers rather than acquisition. Also according to the model, mergers and acquisition, respondent Opinion about M & A, and financial performance were positively correlated with financial performance after merger. A unit increase in mergers and acquisition would lead to increase in application of financial performance by factor of 0.166. This was a clear indication of the firms performing better financially after the resulting merger and/or acquisition. Also the findings concludes that creation of economies of scale, need to gain a higher bargaining power, and business expansions

are the main reasons as to why companies conduct M & A. The study also concludes that despite the process of M & A being smooth and the management orientation remaining the same, still uncertainty and confusion among the employees persist. The study further concludes that merger and acquisition would lead to a high positive performance ($p = 0.02$). Based on the findings the study recommends that there is need for companies to merge to enhance creation of economies of scale, a higher bargaining power, and business expansions.

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CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

In business or economics, a merger is a (commonly voluntary) combination of two companies into one larger company. This involves stock swap or cash payment to the target. Stock swap allows the shareholders of the two companies to share the risk involved in the deal. A merger can resemble a takeover but result in a new company name (often combining the names of the original companies) and new branding. In some cases, terming the combination a “merger” rather than an acquisition is done purely for political or marketing reasons. Examples include the merger of Universal Bank with Paramount Bank and that of the Heritage Insurance Company with Africa International Insurance Company. Mergers and Acquisitions produce synergy, hence better use of complementary resources leading to geographical or other diversification (Gardiner, 2006). This smoothens the earning of a company, which over the long term smoothens its stock price, giving conservative investors more confidence in investing in the company.

An acquisition, also known as a takeover or a buyout, is the buying of one company (the ‘target’) by another. Merger is when two companies combine together to form a new company altogether. An acquisition may be private or public, depending on whether the acquiring or merging company is or not listed in public markets (Eccles, Lanes and Wilson, 1999). An acquisition may be friendly or hostile. Whether a purchase is perceived as friendly or hostile depends on how its communicated and received by the target company's board of directors, employees and shareholders. It is quite normal though for M&A deal communications to take place in a so called 'confidentiality bubble' whereby information flows are restricted due to confidentiality agreements (Harwood, 2006). In the case of a friendly transaction, the companies cooperate in negotiations. In the case of a hostile deal, the takeover target is unwilling to be bought or the target's board has no prior knowledge of the offer. Hostile acquisitions can, and often do, turn friendly at the end, as the acquirer secures the endorsement of the transaction from the board of the acquire company which may require an improvement to the offer made. Acquisition usually

refers to a purchase of a smaller firm by a larger one. Sometimes, however, a smaller firm will acquire management control of a larger or longer established company and keep its name for the combined entity. This is known as a reverse takeover. Another type of acquisition is reverse merger which enables a private company to get publicly listed in a short period of time. This occurs when a private company that has strong prospects and is eager to raise financing buys a publicly listed shell company, usually one with no business and limited assets. Achieving acquisition success has proven to be very difficult, while various studies have shown that 50% of acquisitions were unsuccessful. The acquisition process is very complex, with many dimensions influencing its outcome. There is also a variety of structures used in securing control over the assets of a company, which have different tax and regulatory implications.

Merger is a tool used by companies for the purpose of expanding their operations often aiming at an increase of their long term profitability. Usually, mergers occur in a friendly setting where executives from respective companies participate in a due diligence process to ensure a successful combination of all parts (Bert, 2003). On other occasions, acquisitions can happen through a hostile takeover by purchasing the majority of outstanding shares of a company in the open market.

Managers of firms undertaking mergers and acquisitions often anticipate an improvement in production efficiency. However, such gains to the merging firms do not usually benefit all the stakeholders. For instance, merged firms could easily collude with rival firms and increase prices at the expense of customers. Baldwin, (1998) argues that merged firms may also increase their bargaining power over suppliers by pooling their prices and forcing suppliers to sell their supplies to the combined firm. Higher prices to customers and lower prices charged on supplies imply that the merging firms are able to make higher profits and as a result many mergers are often successful.

Some motives however don't add shareholder value. While diversification for example, may hedge a company against a downturn in an individual industry, it may fail to deliver much value since it's possible for individual shareholders to achieve the same hedge by diversifying their portfolios at a much lower cost than those associated with a merger.

Overextension tends to make the organization fuzzy and unmanageable. Managers' overconfidence about expected synergies from M&A (managers' hubris) may result in overpayment for the target company. In the past, certain executive management teams had their payout based on the total amount of profit made by the company, instead of the profit per share, thus giving the team a perverse incentive to buy companies in order to increase the local profit while decreasing the profit per share hence manager's compensation maybe a setback. Another setback is empire building that involves managers growing big companies in order to have more power but not for economic purpose.

1.1.1 Financial Performance

Financial Performance is one of many different mathematical measures used to evaluate how well a company is using its resources to make profit. Common examples of financial performance measures include operating income, earnings before interest and taxes, and net asset value. Financial performance is a general measure of a firm's overall financial health over a given period of time, and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation or firms performance across time; in this case before and after acquisition.

There are many different ways to measure a company's financial performance. This may be reflected in the firm's return on investment, return on assets, value added among others and is a subjective measure of how a firm can use assets from its primary mode of business to generate revenues. Barber and Lyon (1996) suggest using cash flow based performance measures rather than accounting measures such as return on book value of equity or assets, for studying abnormal operating performance following an event such as post mergers and acquisitions. Besides profits, operating margin defined as operating cash flows divided by net sales can be used to measure financial performance. Operating cash flows are defined as earnings before interest, taxes, depreciation and amortization. As a measure of financial performance, Healy et al., (1992) examined scale operating cash flows by net sales to facilitate comparisons across firms and time periods. They also examined return on capital, book-to-market value of equity and debt-to-equity ratios. Return on capital is net income divided by sum of total equity and debt. Book-to-Market

is the ratio of book value of equity to market value of equity, which is the product of stock price per share and number of stocks outstanding. Debt-to-Equity is the ratio of book value of total debt to book value of total equity.

1.1.2 Oil Industry in Kenya

Oil industry in Kenya is currently dominated by the following major oil companies; Kenya Shell Ltd, Total Kenya Ltd, Kenol/Kobil (Kenya Oil Ltd), Oil Libya Kenya Ltd, National Oil Cooperation (NOC) and Engen. There are other smaller oil companies operating in Kenya, such as Engen, Dalbit, Gapco, Galana, Triton, Petro Oil, Fossil, Oilcom, Hashi Empex, Hass, Global, Addax, Bakri, MGS, Metro, Somken, Gulf Oil and others. There is also a network of independent service station dealers that operate under the umbrella of the Independent Petroleum Dealers of Kenya (Kenya Oil Company Limited, 2008). The major oil companies control about 70% of the market share and own oil infrastructures within the country. For example Kenya shell owns petroleum storage facilities in Nairobi and Mombasa, LPG filling plant in Nairobi and lubricants blending plant in Mombasa.

The oil companies have a distinct brand, which totally differentiates them from the others. For example Kenya Shell, Kenol/Kobil and Total have lubricants and LPG brands that belong to them individually. These brands give them company identity and help them develop brand loyalty among their customer. Oil companies in Kenya also run a nationwide network of retail outlets. For example Kenol/Kobil has 140 service stations in its retail network and holds 20% of the Kenyan fuels market. Kenya Shell runs 130 service stations around the country and commands up to 25% of the Kenyan fuels market. This makes this major oil companies highly visible in the market and differentiates them with others (Price Water House Coppers (PWC), 2010).

Despite Liberalization in 1994, which resulted in increase in number of independent oil distribution companies in Kenya, the major oil companies have maintained their status through acquisitions and mergers. In 2006 Kenya Shell acquired the Share holding of BP in Kenya increasing its market share from 15% to 25% in 2008. Oil Libya acquired Exxon Mobil share

holding in Kenya in 2007. Recently Total Kenya acquired all the assets of Chevron in Kenya (Kenya Oil Company Limited, 2008). In September 2009, Raytec Metals Corporation merged with Lion Petroleum Inc in prospecting oil in two blocks in Mandera area of North Eastern Province (Daily Nation, 2009). Other mergers were those of Kenya Oil Company Limited (Kenol) which merged with Kobil to form Kenol/Kobil Ltd. In 2000, Kenol acquired Galana Oil, petrol and oil vendor.

1.1.3 Mergers and Acquisitions in Kenyan Oil Sector

Mergers and acquisitions (M&A) are a big part of the corporate finance world. A corporate merger is the combination of the assets and liabilities of two firms to form a single business entity. In everyday language, the term acquisition tends to be used when a larger firm absorbs a smaller firm, and merger tends to be used when the combination is portrayed to be between equals. In a merger of firms that are approximate equals, there often is an exchange of stock in which one firm issues new shares to the shareholders of the other firm at a certain ratio. Mergers and acquisitions are aimed at improving profits and productivity of a company. Simultaneously, the objective is also to reduce expenses of the firm (Heyner, 2007).

The energy sector has been an influx in the past three decades, with grand shifts occurring in supply, demand, infrastructure, economics and international competition, which together have created "perfect storm" for realignment and consolidation - and therefore greater mergers and acquisitions activities. The Kenyan oil industry has experienced mergers and acquisitions among various players since the late 90s. Major mergers and acquisitions in the oil industry in Kenya include the Kenol-Kobil merger, Shell-BP, Total Kenya Ltd – Chevron (Caltex) (Nov, 2009) acquisition among others (Njoroge, 2008 and PWC, 2010).

The effects of mergers and acquisitions within the oil industry in Kenya are not well known. Publicly-listed Canadian oil Exploration Company Raytec Metals Corporation has announced that it has entered into negotiations to merge with Lion Petroleum Inc -- the entity that has been allocated the rights by the Kenya government to prospect oil in two blocks in Mandera area of North Eastern Province. A recent entrant into the oil exploration field in Kenya, Lion Petroleum

has production sharing contracts with the government of Kenya on blocks 1 and 2B. The news of the intended merger is the latest in the fast-changing oil exploration landscape in Kenya as response to an increasingly liberalized licensing exploration regime. Until recently, Kenyan authorities were reluctant to approve mergers and farm-ins between oil explorations companies (Daily Nation, 2009). This appears that authorities now realize that as long as the country continues to be regarded as a high-risk exploration frontier, the licensing regime must allow mergers and acquisitions if only to sustain the continued flow of foreign venture capital into the country's oil exploration sector. The subject of the new merger deal between Raytec Metals and Lion Petroleum covers an area of approximately 31,781 square kilometers and is situated west of Mandera Town, extending into Somalia and Ethiopia (Daily Nation, 2009).

The merger will also affect ownership of Block 2B which covers an area of approximately 7,807 square kilometers and borders block 9 where Chinese exploration company CNOOC will shortly commence the drilling of Kenya's first on-shore oil wells in close to 20 years (Daily Nation, 2009). The main objective therefore is to investigate the effects of mergers and acquisitions by undertaking a survey of the oil industry in Kenya. The researcher will be in a position to also establish the influence of mergers and acquisitions on performance of oil companies. The study therefore will add to the body of knowledge since most of the studies done have been in the west (King, et al., 2004 and Galpin and Herndon, 2000) and cannot be generalized to the local situation since business environment is completely different.

1.2 STATEMENT OF THE PROBLEM

The world is in a state of flux, being influenced by the forces of globalization and fast technological changes and as a consequence firms are facing intense competition. To face the challenges and explore the opportunities, firms are going for inorganic growth through various strategic alternatives like mergers and acquisitions (M&A), strategic alliances, joint ventures etc. The M&A are arguably the most popular strategy among firms who seek to establish a competitive advantage over their rivals. Vasilaki and O'Regan (2008) noted that in 2006, globally, the total value of acquisitions undertaken reached unprecedented levels, totaling 1,774 billion.

There are various reasons behind firms going for mergers and acquisitions. The main corporate objectives are to gain greater market power, gain access to innovative capabilities, thus reducing the risks associated with the development of a new product or service, maximize efficiency through economies of scale and scope and finally in some cases, reshape a firm's competitive scope (Hitt et al., 2007). Other reasons include a short-term solution to finance problems that companies face due to information asymmetries (Fluck and Lynch, 1999), revitalize the company by bringing in new knowledge to foster long-term survival (Vermeulen and Barkema, 2001) and to achieve synergy effects (Lubatkin, M. 1987 and Vaara, E. 2002).

Straub (2007) argues that mergers and other types of acquisitions are performed in the hopes of realizing an economic gain. For such a transaction to be justified, the two firms involved must be worth more together than they were apart. Some of the potential advantages of mergers and acquisitions include achieving economies of scale, combining complementary resources, garnering tax advantages, and eliminating inefficiencies. Although all these reasons are meant to increase firm's performance, yet, as Bansal and Kumar (2008) put it, confirmatory research linking merger and acquisition to firm's performance has been little developed. Hence, how mergers influence firms' performance lacks empirical backing as the few studies that have been conducted on the same provide mixed results.

According to Kwoka (2002), mergers have often failed to add significantly to the value of the acquiring firm's shares. Loderer and Martin (1992) studied 304 mergers and 155 acquisitions that took place between 1965 and 1986 and observed a negative but insignificant abnormal return over the five subsequent years after the mergers and positive but insignificant abnormal return for the acquisitions.

Locally studies on mergers and acquisitions have produced mixed results. Katuu (2003) conducted a survey of factors considered important in merger and acquisition decisions by selected Kenyan based firms. Njenga (2006) also conducted a survey on investigation into whether the demerger of coffee marketing societies have created or eroded owners' wealth in parts of Central Kenya. Njenga found mixed results on whether demergers leads to wealth creation or erosion of coffee firms as depicted by both positive and negative returns on post-

merger firms. Muya (2006) carried out a survey of experiences of mergers and found that mergers do not add significant value to the merging firms. Owing to the afore-mentioned mixed and inconclusive results, this study seeks to establish the effect of merger and acquisition on financial performance of oil companies.

1.3 OBJECTIVES OF THE STUDY

The objective of this study was to investigate the effects of mergers and acquisition on the financial performance of Oil companies in Kenya.

1.4 IMPORTANCE OF THE STUDY

As mentioned earlier, very few studies have been conducted on the effects of merger and acquisition besides the same having generated inconclusive and mixed results. This study would, therefore, be of interest to the Scholars, Customers, shareholders, employees, managers and Government.

Scholar-The study would be a source of empirical references and literature and a ground of further research to the scholars.

Customers –mergers can create monopolies and affect customer welfare through reduction of competition and hence unfair prices to the customer. Thus the study will bring out the positives and negatives and enable consumer’s welfare union to air their views when faced with a merger. This will ensure that customers’ interests are taken care of as mergers for monopoly only reduces the value that customers get.

Government - This will help the anti-trust authorities in controlling the activities of mergers.

Shareholders-this will help to widen the knowledge of the stakeholders when faced with decision on mergers and acquisition by analyzing the effects of mergers on financial performance of the firms involved.

The employees will be in a position to establish the stability of the firms and hence their job security.

Managers of various organizations engaging in joint operations will be in a position to highlight the effects that are characteristic of such operations and make wise decisions.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

This chapter summarizes the information from other researchers who have carried out their research in the same field of study.

2.2 THEORIES ON ACQUISITIONS AND MERGER.

Merger refers to the combination of two or more firms, in which the resulting firm maintains the identity of one of the firms, usually the larger. Horizontal merger is an acquisition of a firm in the same industry as the acquiring firm, where the firms compete with each other in their product. Horizontal merger is when two companies competing in the same market merge or join together. This type of merger can either have a very large effect or little or no effect on the market. When two extremely small companies combine, or horizontally merge, the results of the merger are less noticeable. These smaller horizontal mergers are very common. If a small local drug store were to horizontally merge with another local drugstore, the effect of this merger on the drugstore market would be minimal. In a large horizontal merger, however, the resulting ripple effects can be felt throughout the market sector and sometimes throughout the whole economy.

Large horizontal mergers are often perceived as anticompetitive. If one company holding twenty percent of the market share combines with another company also holding twenty percent of the market share, their combined share holding will then increase to forty percent. This large horizontal merger has now given the new company an unfair market advantage over its competitors.

All companies are subject to Federal laws that prohibit certain actions from taking place during a horizontal merger. When a horizontal merger takes place, the loss of a competitor in the market creates benefits for the companies that merged; while at the same time serves to drive prices up for the consumer. Federal laws protect the consumer. Examples of horizontal mergers are:

Daimler –Benz and Chrysler which merged to form Daimler Chrysler. Exxon and Mobil, which merged to form Exxon Mobil. Volkswagen and Rolls Royce and Lamborghini, Ford and Volvo, Disney and Miramax, Bell Atlantic and GTE corporation to form Verizon, Shell-BP, PricewaterhouseCoopers GlaxoSmithKline Plc, Aon Minet, Kenya Oil Co. Ltd and Crown Berger.

Economists have promoted several competing theories of M&As. Among them are empire-building (Baumol, 1967), furthering anti-competitive activities, such as monopoly power (Mueller, 1993), management-entrenchment (Shleifer and Vishny, 1989), and an overestimation of a manager's ability to improve the performance of a target he or she perceives to be underperforming (Roll, 1986). The other theory is of is that inefficient plants and firms are taken over and efficient firms survive (Manne, 1965). Theories of M&As are not mutually exclusive. A firm could, for example, seek to gain market power and at the same time be building an empire and believe that it can more efficiently manage the business of a firm or plant it has targeted as a potential acquisition.

Various reasons for why firms merge have been proposed. The list includes efficiency-related gains, disciplining target management, spreading new technology, and changes in industry structure. While there is an ongoing debate about the merits and deficiencies of each of the proposed explanations of mergers, there seems to be a consensus on some important aspects of merger activity: mergers happen in waves and, within each wave; they tend to cluster by industry. Yet, why this is the case remains an open question. Brealey, Myers and Allen (2006) go so far as to suggest that why merger waves occur is one of ten most important unresolved questions in corporate finance. Several theories have been put forward to explain merger waves. Lambrecht (2004) examines mergers motivated by operational synergies and predicts pro-cyclical mergers. In his model, mergers are likely to happen in periods of economic expansion.

Maksimovic and Phillips (2001) show that mergers and asset sales are more likely following positive demand shocks, causing pro-cyclical merger and acquisition waves in perfectly competitive industries. In their paper, higher quality firms buy lower quality ones when the marginal returns from adding capacity are great enough to outweigh decreasing returns to

managerial skill. In Lambrecht and Myers (2006), takeovers serve as a mechanism to force disinvestment in declining industries. Their arguments lead to takeover transactions occurring mostly in industries that have experienced negative economic shocks. Some recent papers link takeover activity to stock market misvaluation. In Shleifer and Vishny (2003), rational managers exploit the misvaluation of less-than-rational investors. Rhodes-Kropf, Robinson and Viswanathan (2006) show theoretically and empirically that merger activity is correlated with high market valuations, causing overvalued bidders to make stock bids that are more likely to be accepted by targets

2.2.1 Corporate Control Theory and M&As

Corporate control theory (Jensen, 1988 and Shleifer and Vishny, 1988) argues that takeover is an efficient means to replace inefficient managers of target companies. The target firm may underperform either because its managers pursue their own interests at the expense of owners' interests or because they lack the knowledge and skills to maximize firm value. If managers of acquiring firms are more capable than those of acquired firms, they can improve the efficiency of targets. This theory predicts that poorly performing firms are more likely to be acquired and that the performance of targets will improve after the takeover. Acquiring firms are also expected to gain from the takeover activity if they have the ability to bring operating synergy to the post-takeover entity.

2.2.2 Financial Synergies and M&As

M&As also can be motivated by financial synergies. Financial synergy theory argues that, with asymmetric information in financial markets, a firm with insufficient liquid assets or financial slack may not undertake all valuable investment opportunities (Myers and Majluf, 1984). In this case, the firm can increase its value by merging with a slack-rich firm if the information asymmetry between the two firms is smaller than that between the slack-poor firm and outside investors. Thus, takeover may be an efficient means to alleviate information asymmetries and achieve financial synergies. This theory predicts that firms in financial distress but with good

investment opportunities are more likely to be involved in M&A activities, either as targets or as acquirers.

2.2.3 Agency Costs and M&As

The agency cost theory of M&As argues that takeover activity often results from acquiring firm managers' acting in their own self-interests rather than in the interests of the firm's owners (Shleifer and Vishny, 1988 and 1989). Managers may be motivated to increase their compensation by increasing the size of the firm through non-value enhancing mergers or engaging in "expense preference" behavior by over-consumption of perquisites. Managers also may intentionally acquire businesses that require their personal skills in order to make it costly for shareholders to replace them. To the extent that M&As are primarily motivated by managerial self interest, they are unlikely to generate operating or financial synergies that lead to improvements in efficiency or productivity.

2.2.4 Managerial Hubris and M&As

According to the managerial hubris hypothesis, even if managers try to maximize the value of the firm, they might overestimate the value of what they buy because of hubris (Roll, 1986). This is particularly true in waves of consolidation, when managers blindly follow the markets and change their beliefs on conglomeration versus strategic focus or when multiple bidders compete for the same target. Managers also could underestimate the cost of post-merger integration or overestimate their ability to control a larger institution. Thus, a transaction that is believed to benefit the acquirer could simply be a poor strategic decision where benefits are overestimated or costs are underestimated.

2.2.5 Industry Shock Theory and M&As

Industry shock theory holds that M&A activities within an industry are not merely firm-specific phenomena but the result of the adaptation of industry structure to a changing economic environment or "industry shocks" such as changes in regulation, changes in input costs, increased foreign or domestic competition, or innovations in technology. Mitchell and Mulherin

(1996) argue that corporate takeovers are the least costly means for an industry to restructure in response to the changes brought about by economic shocks but that post-takeover performance of firms should not necessarily improve, compared to a pre-shock benchmark.

2.3 TYPE OF MERGERS AND ACQUISITIONS

Merges can be classified in three broad categories. Horizontal mergers are mergers between two or more firms in the same industry. Companies in the same line of business often look for various strategies to remain on the competitive edge. Such companies explore strategic alliances, which would grow their business and keep them afloat. Such strategic alliances include horizontal mergers, which have become quite common in the banking industry, financial services sector, telecom industry and in the pharmaceutical industry as is the case of GlaxoSmithKline. In a horizontal merger, the acquisition of a competitor could increase market concentration and increase the likelihood of collusion. The elimination of head-to-head competition between two leading firms may result in unilateral anticompetitive effects (Scherer, 1988).

Vertical mergers represent combinations between firms in which supplier or buyer relationships may exist. Such mergers will occur where a big manufacturing company may form a strategic alliance with the firms, which supplies its raw materials, or does its distribution, mainly driven by the desire to drive down costs, or ensure undisrupted supply of raw materials or supply chain. Vertical mergers are common in the manufacturing industry, given the whole relationship between raw materials, warehousing, manufacturing and distribution (Samuels, 2005).

A vertical merger can harm competition by making it difficult for competitors to gain access to an important component product or to an important channel of distribution. Take the merger of Time Warner, Inc., producers of HBO and other video programming, and Turner Corp., producers of CNN, TBS, and other programming. There was concern that Time Warner could refuse to sell popular video programming to competitors of cable TV companies owned or affiliated with Time Warner or Turner -- or offer to sell the programming at discriminatory rates. That would allow Time Warner-Tuner affiliate cable companies to maintain monopolies against competitors like Direct Broadcast Satellite and new wireless cable technologies. What's more,

the Time Warner-Turner affiliates could hurt competition in the production of video programming by refusing to carry programming produced by competitors of both Time Warner and Turner. The FTC allowed the merger, but prohibited discriminatory access terms at both levels to prevent anticompetitive effects (Samuels, 2005, Mueller, 1993 and Muya, 2006).

The third category of mergers is that of conglomerates. Conglomerate mergers occur among firms in different lines of business. A merger between a bank and a telecom company would be seen as a conglomerate since these are two companies, in different industries, merging for some strategic benefits. Conglomerate mergers often result into big monopolies, which if not well regulate can kill competition and create huge companies which become economic powers in the world (Mueller, 1993 and Marsh, Siegel and Simons, 2007).

2.4 EMPIRICAL EVIDENCE

Andre, Kooli and L'Her (2004) studied the long-term performance of 267 Canadian mergers and acquisitions that took place between 1980 and 2000, using different calendar-time approaches with and without overlapping cases. Their results suggested that Canadian acquirers significantly underperform over the three-year post-event period. Further analysis showed that their results are consistent with the extrapolation and the method-of-payment hypotheses, that is, glamour acquirers and equity financed deals underperform. Andre, Kooli and L'Her also found that cross-border deals perform poorly in the long run.

Franks, Harris, and Titman (1991) studied companies' performance following corporate takeovers of 399 acquisitions during the 1975-1984 periods. The study used multifactor benchmarks from the portfolio evaluation literature that overcome some of the known mean-variance inefficiencies of more traditional single-factor benchmarks. After adjusting for systematic risk and size, but not for the book-to-market ratio, they found positive and significant long-term abnormal returns only for small transactions. The study concluded that previous findings of poor performance after takeover were likely due to benchmark errors rather than mispricing at the time of the takeover.

Loderer and Martin (1992) studied the post-acquisition performance of acquiring firms of 304 mergers and 155 acquisitions that took place between 1966 and 1986. They observe a negative but insignificant abnormal return over the five subsequent years (significant when measured over three years) for the mergers and positive but insignificant abnormal return for the acquisitions. They observed evidence of negative performance in the second and third post-acquisition years, but that performance occurs mainly in the 1960s and 1970s, and disappears in the 1980s. Thus, especially in the later years, the post-acquisition years do not provide convincing evidence of wasteful corporate acquisitions, or strong evidence that contradicts market efficiency.

Palia (1993) identifies financial, regulatory, and managerial factors that impact the level of bank merger premiums. The managerial factors include the equity ownership of the acquiring bank's management and the equity ownership of the target bank's management. Palia finds financial factors related to loan quality and market power are positively related to merger premiums and negatively related to the relative size of the participants, suggesting a lack of opportunities to realize economies of scale or scope when acquiring a relatively large bank. All three regulatory factors are statistically significant and are positively related to merger premiums. This suggests that a protective regulatory environment for the target bank is potentially more valuable to the acquirer. Palia also identifies a non-linear relationship between the management ownership values and merger premiums. For acquirers, the results exhibit a U-shaped relationship between merger premiums and the acquirer's management ownership, implying potential agent-owner conflicts. For targets, an inverted U-shaped relationship exists between merger premiums and the target's management ownership. Consistent with an earnings diversification hypothesis related to mergers, Benston, Hunter, and Wall (1995) studied how mergers and acquisitions in banking industry are motivated by enhancing earnings diversification. They found that bid premiums were negatively related to the variances and covariances of the bidder's and target's returns on assets and relative size, as well as positively related to the capital-to-assets and market-to-book value ratios.

Agrawal, Jaffe and Mandelker (1992) examined the post-merger performance of acquiring firms. find negative and significant abnormal returns for 937 mergers over the five subsequent years, and positive but insignificant abnormal returns for 227 tender offers that occurred between 1955

and 1987. Ansof, Bradenburc, Porter and Radosevlch (1971) found that after an acquisition, low sales growth companies showed significantly higher rates of growth, whereas, high sales growth companies showed lower rates of growth. However, even though low sales growth companies showed higher rates of growth after acquisitions, they actually suffered decreases in their mean P/E ratios, mean EPS and mean dividend payouts. The similar pattern of inconsistency found in the high sales growth companies whereby their performance levels for EPS, PE ratio, earnings and dividend payouts were greater. Low sales growth companies financed their acquisitions through decreased dividend payouts and the use of new debts. In contrast, high sales growth companies with other strategies tended to decrease debts but increase dividend payouts. Acquisitions were in general unprofitable, as they did not contribute to increases in all of the variables of the companies' growth. Acquiring firms registered lower rates of growth as compared to the non-acquiring firms and this was more pronounced for low sales growth acquiring firms.

Firm size and financial performance of acquiring firms can be the determinants of poor performance in the post-acquisition period (Schmidt, Dennis, Fowler and Karen, 1990). Investors do not hold more favourable expectations for related mergers than for unrelated ones and stockholder value appreciates most for vertical mergers. Hence, acquisition involving vertical integration creates more value to large companies (Lubatkin, 1987) despite the findings of many studies concluded that firms participated in related acquisitions experienced superior economic returns in comparison with unrelated acquisitions. Hence, the rationale for the superior economic performance was due to the synergetic effect especially via complementary resources.

Ingham, Kiran and Lovestam (1992) studied the relationship between mergers and firm profitability by surveying 146 of the UK's top 500 companies. The study revealed that is the expected reward of increased profitability which has driven the takeover market and that it is this traditional measure which is used in ex-post evaluation. According to the findings, managers firmly perceive that their takeover activity had been performance enhancing for their company. The evidence presented did suggest that the integration of small acquisitions into an existing organizational structure may be achieved without severe problems of loss of control, and the subsequent decline in performance which beset large acquisitions.

Allen (1990) investigated whether excessive premiums for acquisitions dilute performance and reiterated that an acceptable premium should be no more than the discounted cash flows of a firm, as adjusted for any efficiencies or synergies the acquisition would exploit. In the Asian context, most value creation (cost reduction) materialized from either worker layoffs or renegotiating supplier contracts during the merger process.

Firth (1979) examined merger and takeover activity in the United Kingdom specifically, the impact of takeovers on shareholder returns and management benefits was analyzed, and some implications for the theory of the firm are drawn from the results. The study showed that mergers and takeovers resulted in benefits to the acquired firms' shareholders and to the acquiring companies' manager, but that losses were suffered by the acquiring companies' shareholders. The results were consistent with takeovers being motivated more by maximization of management utility reasons, than by the maximization of shareholder wealth.

Muthiani (2007) studied the cross cultural perspective of mergers and acquisitions done by GlaxoSmithKline Kenya PLC (GSK) by conducting the study on the 50 senior and middle managers at GSK. It was established that the GSK's staffs were highly motivated and performance driven inherent from organizational culture evolving from the merger. The study thus concluded that culture is a very important element for the success of merger as it is also a key to success of a business and a good culture also leads to better performance of a business.

Muchae (2010) studied challenges of cross border mergers and acquisitions and the factors influencing the same in Tiger Brands Limited. Muchae found that performance related factors such as perceived synergies, wider product scope, and new market for products were the driving factors for merger and acquisition of Tiger Brands Limited (HACO). The study however found that following acquisition the staff were less motivated with loss of incentives and there uncertainty regarding their job security and challenges experienced in bedding down the new structure were such as redundancy which was were addressed by offering retirement package and excess capacity was deployed which negated performance. Chesang (2002) studied how merger commercial banks in Kenya influence their financial performance. Chesang found that firm size and financial performance of acquiring firms can be the determinants of poor performance in the

post-acquisition period. Muya (2006) carried out a survey of experiences of mergers and found that mergers do not add significant value to the merging firms. Njenga (2006) also conducted a survey on investigation into whether the demerger of coffee marketing societies have created or eroded owners' wealth in parts of Central Kenya. Njenga found mixed results on whether demergers leads to wealth creation or erosion of coffee firms as depicted by both positive and negative returns on post-merger firms.

2.5 CONCLUSIONS

There are several theories that explains mergers and acquisitions which are corporate control theory which argues that mergers and acquisitions are conducted to replace inefficient managers of target companies, financial synergy which portends that firm with insufficient liquid assets or financial slack can increase its value by merging with a slack-rich firm which would put it in a good position to take valuable investment opportunity (Myers and Majluf, 1984 and Jensen, 1988). Agency cost theory argues that through self interests managers, motivated to increase their compensation, can increasing the size of the firm through non-value enhancing mergers which will unlikely generate operating or financial synergies that lead to improvements in efficiency or productivity (Shleifer and Vishny, 1988).

According to the managerial hubris hypothesis, owing to poor judgment acquisition could simply be a poor strategic decision where benefits are overestimated or costs are underestimated (Roll, 1986). Industrial shock theory puts it that while mergers and acquisition can be undertaken as a less costly means for an industry to restructure in response to market or economic changes, post-takeover performance of firms should not necessarily improve, compared to a pre-shock benchmark (Mitchell and Mulherin, 1996).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 INTRODUCTION

This chapter sets out various stages and phases that were followed in completing the study. It involves a blueprint for the collection, measurement and analysis of data. This section is an overall scheme, plan or structure conceived to aid the researcher in answering the raised research question. In this stage, most decisions about how research was executed and how respondents were approached, as well as when, where and how the research was to be completed. Therefore in this section the research identified the procedures and techniques that were used in the collection, processing and analysis of data. Specifically the following subsections should be included; research design, target population, data collection instruments, data collection procedures and finally data analysis.

3.2 RESEARCH DESIGN

This study took on a causal research design. Gay and Airasian (2003) note that causal research designs are used to determine the causal relationship between one variable and another; in this case, the cause and effect relationship between merger and acquisition on the performance of oil companies in Kenyan. Causal research design is consistent with the study's objective which is to determine the effect of mergers and acquisition on long-run profitability, leverage and liquidity position of oil firms in Kenya.

3.3 POPULATION

Target population in statistics is the specific population about which information is desired. According to Mugenda and Mugenda (2003), a population is a well defined or set of people, services, elements, events, group of things or households that are being investigated. This definition ensures that population of interest is homogeneous. And by population the researcher means complete census of the sampling frames. In this study, the target population was the oil

companies in Kenya that have conducted merger and acquisitions. In Kenya, some of the companies that have undergone merger and acquisition include Shell-BP, Kenol-Kobil, Raytec Metals Corporation with Lion Petroleum and an acquisition involving Total Kenya Ltd acquiring Chevron Company Ltd trading as Caltex in Kenya. Therefore the target population was for oil companies that had experienced merger and acquisition. The study considered all the companies targeted and census was used in selecting 10 respondents from each company to make an aggregate sample.

3.4 DATA COLLECTION

In order to establish the effects of Merger and Acquisitions at the Kenya Oil Industries, self-administered drop and pick questionnaires were distributed to randomly picked management staff of the oil companies in Kenya that have conducted mergers and acquisitions. In order to collect primary data, questionnaires were designed to establish the effects of mergers and acquisition at Kenya oil industries. The questionnaires were semi-structured; that is, had both open-ended and closed-ended questions. These questionnaires were distributed to the respondents through direct administration to the staff. Secondary data sources were also employed through the use of previous documents or materials to supplement the primary data received from the respondents. The secondary data collected was on the return on equity and asset, liquidity ratio and profitability.

3.5 DATA ANALYSIS

After the questionnaires were sent and before processing the responses, the completed questionnaires were edited for completeness and consistency. A qualitative analysis was employed. The qualitative analysis was used to analyze the respondents' views about the effects of mergers and acquisition in Kenya oil industry. Qualitative data analysis makes general statements on how categories or themes of data are related (Mugenda and Mugenda, 2003). The qualitative analysis was done using content analysis. Content analysis is the systematic qualitative description of the composition of the objects or materials of the study (Mugenda and Mugenda, 2003). It involves observation and detailed description of objects, items or things that

comprise the object of study. The data collected under the questionnaire was analyzed using descriptive statistics. The data was entered and coded into the Statistical Package for Social Sciences (SPSS version 17). The basis of using descriptive measure was to give a basis for determining the weights of the variables under the study. The findings then presented using tables, pie charts, and bar graphs for easier interpretation.

The study also established the association between pre-and post-merger or acquisition performance by using chi-square. The Chi-Square test is used to determine whether an association (or relationship) between 2 variables in a sample is likely to reflect a real association between these 2 variables in the population or if there is a difference between the two variables. It thus test the probability (p-value) that the observed association between the 2 variables has occurred by chance, i.e. due to sampling error

In this case, the hypothesis was that:

H₀: Merger and acquisitions is not associated with increase in financial performance

This hypothesis was tested at 0.05 significance level.

The study also used linear regression model in analyzing the effect of merger and acquisition on the financial performance of companies listed in at the NSE. The regression model was of the form: $Y = \beta_0 + \beta_1X_1 + \beta_2X_2\dots\dots+ \varepsilon$

Whereby Y is the independent variables, β_0 is the regression constant or Y intercepts, $\beta_1\dots \beta_x$ are the coefficients of the regression model and ε is the error term which is signified by the model's significance. The basis of the model is to help in measuring financial performance by exploring the contribution of various components such as revenue and liquidity that affects measures of financial performances which include return of equity, return on investment and return on assets.

Given that merger and acquisition, as explained in the previous chapters, put companies in a good stead for sales turnover through better bargaining power and market share; mergers and acquisitions affects a company's Return on Equity (ROE) and liquidity state. From the foregoing, the regression model was

$$ROE = \beta_0 + \beta_1 \text{Sale} + \beta_2 \text{Liquidity} + \varepsilon$$

Y was the Return on Equity (ROE), Sales turnover and liquidity which was computed as the ratio of Liability to assets.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION OF RESULTS

4.1 INTRODUCTION

This chapter presents analysis of the data found. The study used purposive sampling technique to come up with a sample of 30 respondents from which all the questionnaires were filled in and returned making a response rate of 100%. This response rate was excellent, representative and conforms to Mugenda and Mugenda (2003) stipulation that a response rate of 50% is adequate for analysis and reporting; a rate of 60% is good and a response rate of 70% and over is excellent.

4.2 BIO-DATA

4.2.1 Gender of the respondent

This study sought to establish the proportions of the employees working in this company based on their gender. The data finding were recorded in the figure 1 below.

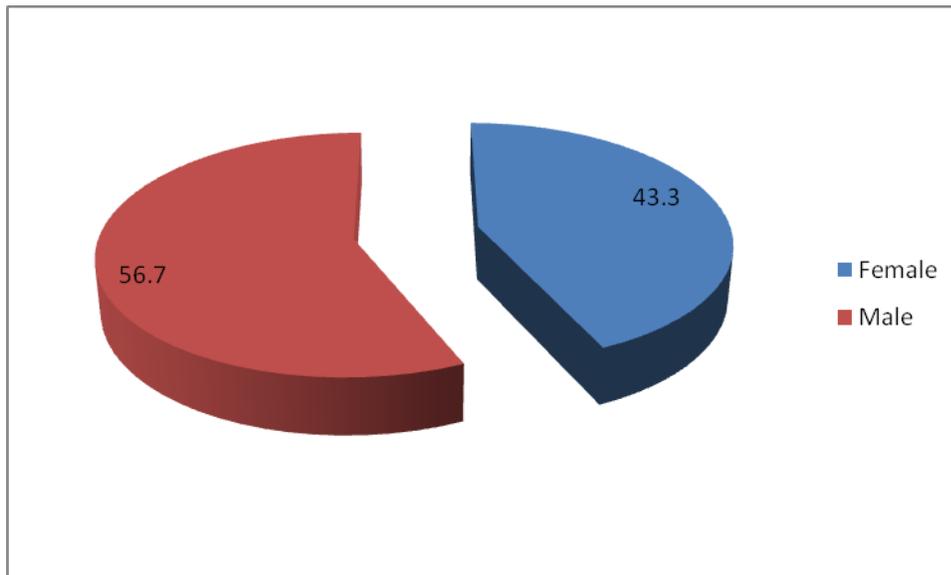


Figure 1: Gender

From the table above 56.7% of the respondents were male while 43.3% were female. This illustrates that oil companies in Kenya employs slightly more men to women.

4.2.2 Duration working at the company

The study also sought to establish the length of time the respondents had worked in the company. According to the data findings in table 1, 40% of the respondents had worked in the company for 6 to 10 years, 33.3% had worked there for 1 to 5 years, 23.3% had worked there for between 11 and 15 years and only 3.4% had worked there for 16 to 20 years. This indicated that majority of the respondent had worked in the company for more than 6 years. This depicts that they had interacted with the company for long enough and therefore the information they would give would be reliable.

4.2.3 Respondents' Level of Management

In this study the researcher aimed at establishing the level of management held by the respondents in the company. The data findings were presented in the figure 2 below.

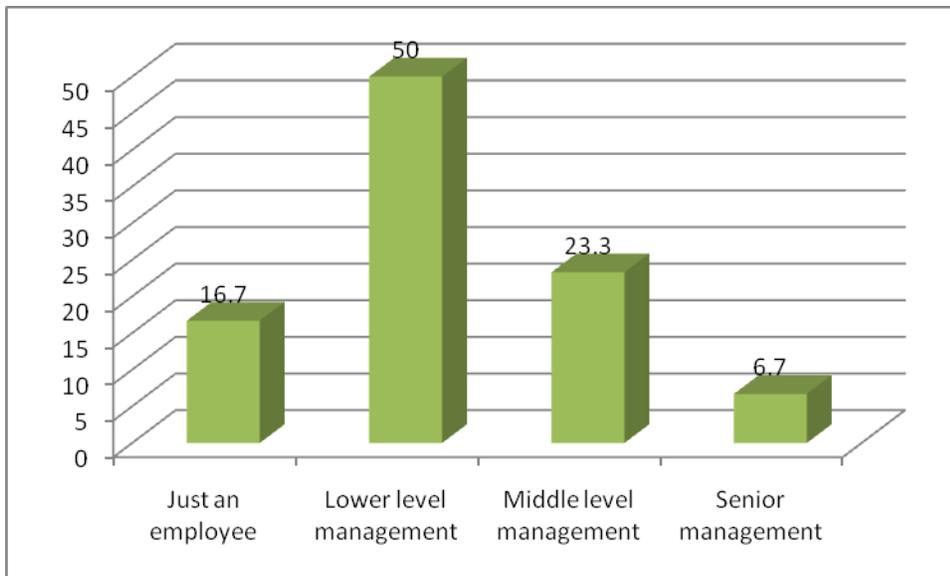


Figure 2: Respondents' Level of Management

50% of the respondents were in the lower level management, 23.3% were in the middle level management, 16.7% were just employees and only 6.7% were in senior management. It therefore illustrates that majority of the respondents were at least in the lower level management. This means that the respondents were in a position to give valuable information owing to the positions held.

4.3 ORGANIZATION CORPORATE ACTION (MERGER OR ACQUISITION)

4.3.1 Nature of organization corporate action

The study also aimed at finding out the nature of organization corporate action involved during formation. Figure 3 below presents the data finding on this.

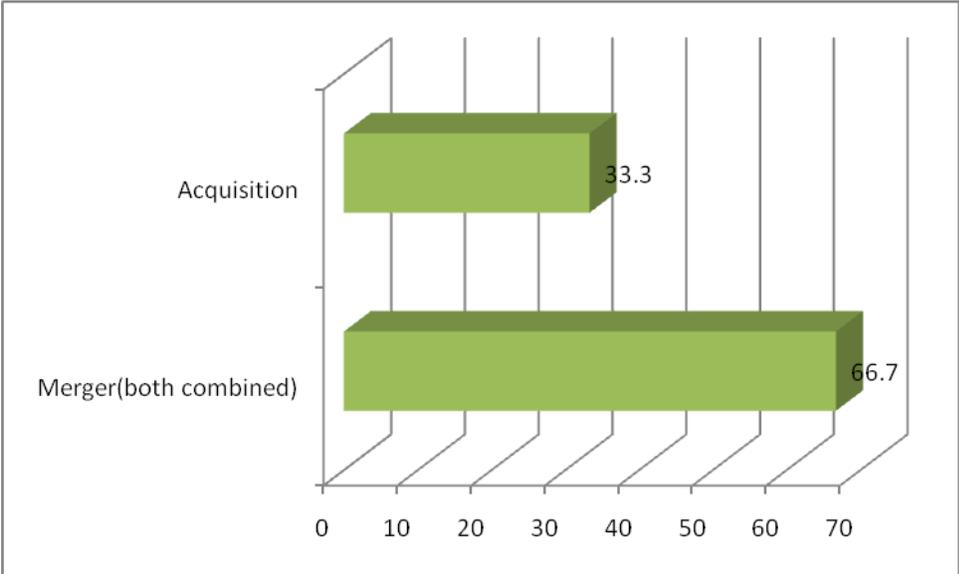


Figure 3: Nature of organization corporate action

According to the table above, 66.7% of the organizations were formed through merger (both combined) and 33.3% were through acquisition. It therefore depicts that majority of these organization were established through mergers, where both organizations combine together to combine synergies and form one firm as opposed to one firm completely acquiring the other.

4.3.2 Employment period for the respondent

This study also sought to establish which company the respondent was working before the merger or acquisition. The data findings were presented in the figure 4 below.

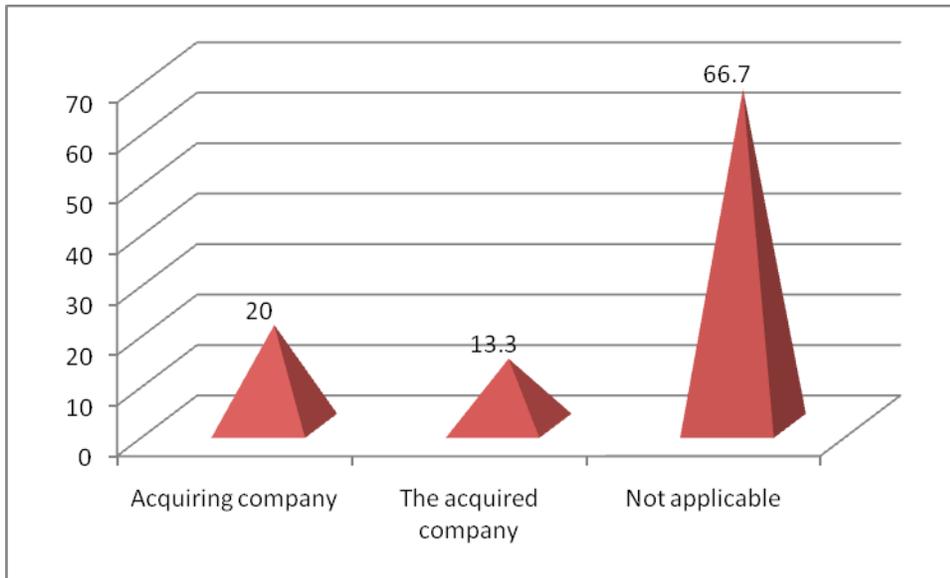


Figure 4: Employment period for the respondent

66.7% of the respondents were not working with the company during the time of merger/acquisition, 20% of the respondents were in the acquiring company while only 13.3% were in the acquired company. This implies that majority of the employees in the company got their jobs after the merger/acquisition.

4.3.3 Mergers and Acquisition (M&A)

The study sought to establish the relevance of various statements in relation to mergers and acquisition (M & A) and the results were presented in table 2. According to the findings, The companies created M & A to create economies of scale and M & A was driven by need to gain a higher bargaining power, were found to be the most important reasons given by respondents for mergers and acquisition of their companies as shown by a mean of 4.60. M&A was driven by

need for business expansions with a mean score of 4.57 and a standard deviation of 0.496. The company's profitability increased upon a merger, M&A was driven by globalization, M&A was driven by cost project to be undertaken, The companies conducted the M&A to create quality of service, The companies conducted M&A to create more efficiency, Mergers and acquisition(M&A) occurred to create monopolies and fight competition, The companies conducted M&A to deploy idle resources, and Employees were given top priority during mergers were other reasons with mean scores of 4.23, 4.07, 4.00, 4.00, 3.80, 3.63, 2.97 and 2.73 respectively as perceived by the respondents which were considered during mergers and acquisition. These findings therefore indicate that creation of economies of scale, need to gain a higher bargaining power, and need for business expansions were the major reasons which drove the companies to create mergers and Acquisitions.

4.3.4 Respondent Opinion about M & A

The study further sought to establish the opinion of the respondents with regard to M & A in their companies and the results were presented in table 3. According to the findings, "as far as I am concerned, the process is smooth" was found to be the most important opinion in relation to M & A. with a mean of 1.900. I felt uncertain and confused, management orientation remained the same, behavioral tendencies have remained the same, I experienced no difference on my work, the values of the organization remained the same, work procedures and processes remained the same, I received adequate information on what was going to happen, I received regular updates on what was happening, I clearly understood the implications of the merger process" were the other opinions given with regard to M & A in companies with means of 1.767, 1.667, 1.633, 1.600, 1.567, 1.500, 1.333, 1.300, and 1.233 respectively.

4.3.5 Relevance of statement to M & A.

The study further sought to establish the relevance of various statements about the merger or acquisition of the company the respondent worked for and the results were presented in table 4.

From the findings, “both companies had similar approach to rewards” was found to be the most important statement in relation to M & A with a mean of 1.900 and a standard deviation of 0.300. “Companies had similar approach to promotions, both companies had similar approach to recruitments and both companies had similar decision making process were the other statement given for M & A in companies with means of 1.767, 1.733 and 1.433 respectively.

4.4 RELATIONSHIP BETWEEN PRE AND POST-MERGER OR ACQUISITION PERFORMANCE.

The study sought to establish the association (significance) between the means of the pre and post-merger and acquisition performances of oil companies in Kenya using chi-square. The study used a five-year average annual profitability of the oil companies, pre-and post merger.

| | Value | df | Asymp. Sig. (2-sided) |
|--------------------|--------------|-----------|------------------------------|
| Pearson Chi-Square | 20.000a | 16 | .0202 |
| Likelihood Ratio | 16.094 | 16 | .0464 |
| N of Valid Cases | 5 | | |

a. 25 cells (100.0%) have expected count less than 5. The minimum expected count is .20.

According to the findings in the above table, the significance figure was 0.0202, which shows that there was a statistically significant relationship between pre and post-merger and acquisition performances of oil companies. This is because the significance figure was less than 0.05 ($p \leq 0.05$).

4.5 EFFECT OF MERGER AND ACQUISITION ON THE FINANCIAL PERFORMANCE

The study also used linear regression model in analyzing the effect of merger and acquisition on the financial performance of companies listed in at the NSE. The regression model was of the form: $Y = \beta_0 + \beta_1X_1 + \beta_2X_2 \dots + \varepsilon$

Whereby Y is the independent variables, β_0 is the regression constant or Y intercepts, $\beta_1 \dots \beta_x$ are the coefficients of the regression model and ε is the error term, which is signified by the model's significance.

4.6 REGRESSION ANALYSIS

Table 4.1: ANOVA Statistics

| | | | | | |
|----------------------------|----------------|---------|-------------|-------|------|
| Model | | | | | |
| R | | .789 | | | |
| R Square | | 0.889 | | | |
| Adjusted R Square | | 0.394 | | | |
| Std. Error of the Estimate | | 0.23173 | | | |
| | Sum of Squares | df | Mean Square | F | Sig. |
| Regression | 73427.43 | 5 | 45325.45 | 0.136 | .001 |
| Residual | 45362.81 | 25 | 4340.836 | | |
| Total | 114359.24 | 30 | | | |

From the ANOVA statics in table 4.5, the processed data, which are the population parameters, had a significance level of 2% that shows that the data is not ideal for making a conclusion on the population's parameter. The R is known as correlation value that shows the strength of relationship between independent and dependent variable. From the above table there was strong relationship between merger and acquisition and financial performance of listed companies as shown by correlation factor of 0.789.

The adjusted R^2 is known as coefficient of determination and it shows the variation in effect of merger and acquisition and financial performance. From the above table there was 39.4% variation in merger and acquisition and financial performance of listed companies.

Table 4.2: Coefficients of Results

| Model | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|--------------------------------|-----------------------------|------------|---------------------------|--------|-------|
| | B | Std. Error | Beta | | |
| (Constant) | 1.465 | 4.984 | | 0.896 | 0.122 |
| Mergers and Acquisition | 0.166 | 2.97 | 0.059 | 0.393 | 0.698 |
| Respondent Opinion about M & A | -0.925 | 5.349 | -0.278 | -1.669 | 0.107 |
| Financial performance | 0.944 | 2.774 | 0.136 | 0.701 | 0.489 |

The coefficient table in table 4.6 above was used in coming up with the model below:

$$Y = 1.465 + 0.166 X_1 - 0.925X_2 + 0.944 X_3 + 0.171 X_4$$

According to the model, mergers and acquisition, respondent Opinion about M & A, and financial performance were positively correlated with financial performance after merger. A unit increase in mergers and acquisition would lead to increase in application of financial performance by factor of 0.166. The coefficient of respondent opinion about merger and acquisition is quite low and thus insignificant which might have been as a result of different experiences during the mergers/acquisition. Overall mergers and acquisition and financial performance coefficients are significant indicating firms performing better financially after the resulting merger and/or acquisition.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATION

5.1 INTRODUCTION

This chapter presents discussions of the key findings presented in chapter four, conclusions drawn based on such findings and recommendations there-to. This chapter will thus be structured into summary of findings, conclusion and recommendations, limitations of the study and areas for further research. This chapter summarizes key findings and draws conclusions relevant to the research. From the analysis and data collected, the following summary of findings, conclusions and recommendations were made.

5.2 SUMMARY OF FINDINGS AND DISCUSSIONS

From the findings that majority of the respondents had worked in the company for more than 6 years and most respondents were in at least lower management level. This meant that the respondents were in a position to give knowledgeable, accurate and valuable information owing to the positions held and long interaction with the company. According to the findings, majority of these companies were established through mergers rather than acquisition. Merger occurs when two companies combine together to form a new company while an acquisition is the buying of one company by another. This is so because the process of merger involves both companies retaining their identity without fear of being swallowed by the other. Also the process of merger aims at strengthening both companies involved and hence the resistance is quite minimal as employees and all the parties involved will be part of the new entity. On the other hand acquisition also known as takeover can either be friendly or forced meaning it is for survival. Company being acquired means loss of identity and there is a lot of resistance from interest groups involved in the deal. Looking at the two scenarios involving merger and

acquisition deals it is correct to back the finding that majority of the companies are formed through merger rather than acquisition.

On which company the respondent was working before the merger or acquisition, the study found that majority of the employees in the company got their jobs after the merger/acquisition. The process of merger/acquisition involves a lot of negotiations and compensation deals. Companies involved in merger/acquisition deals often give an attractive compensation package in order to cut on the number of the employees for the merged company and also to reduce the wage bill by allowing high earning employees to leave the company through that compensation process. In this process more employees leave necessitating need for new employees. For example in the case of Total Kenya acquiring Chevron most Chevron employees opted for compensation rather than joining Total.

According to the findings creation of economies of scale, need to gain a higher bargaining power, and need for business expansions were the major reasons which drove the companies to create mergers and Acquisitions. As a result of increase in cost of running the business and increased competition companies look for strategies that will keep them afloat through strategic alliances such as merger and acquisition. When two companies merge economies of scale are created through use of same production plant, a cut down on distribution costs through use of one network and many others. Companies merge in order to improve their competitive advantage by marshalling together massive resources hence higher bargaining power. Acquisition of Chevron by Total Kenya was a key strategy meant to give Total competitive advantage by acquiring strategic petrol stations for distribution purposes and the blending plant located in Mombasa.

M & A for deploying idle resources were least considered during mergers and acquisition. Most mergers and acquisition are not based on need to utilize idle resources because in most cases companies are undercapitalized and because the process of getting additional capital is tedious

and costly then companies opt for these strategies in order to combine the already over stretched resources.

On the different opinions of the respondents with regard to different statements about M & A in their companies, “As far as I am concerned, the process is smooth, was found to be the most important statement in relation to M & A. “I felt uncertain and confused, management orientation remained the same, behavioral tendencies have remained the same, I experienced no difference on my work, the values of the organization remained the same, work procedures and processes remained the same, I received adequate information on what was going to happen, I received regular updates on what was happening, I clearly understood the implications of the merger process” were the other statements in order of importance with regard to M & A in companies .All this shows that when mergers and acquisition are taking place the preoccupation is on the benefits to be achieved and the negotiations are between the owners with the employees expected to buy in to the idea already decided. Furthermore ownership decisions lie with shareholders not the employees and their work is to implement shareholders decisions.

The study further found out that on the relevance of various statements concerning merger or acquisition of the company to the respondents, “both companies had similar approach to rewards” was found to be the most important statement in relation to M & A. “Both companies had similar approach to promotions, both companies had similar approach to recruitments and both companies had similar decision making process were the other statement given for M & A in companies. The study further found that there is a significant relationship between pre and post-merger financial performance of oils companies ($p < 0.05$).

5.3 CONCLUSIONS AND RECOMMENDATIONS

Based on the findings, the study shows that oil companies employ more men than women and most employees are there for a period of 1-10 years indicating high rate of employee turnover in the industry. It can also be concluded that merger is a common method of business combination compared to acquisition which can be explained by the fact that merger involves joining of the

companies involved as equals or in slight difference without loss of identity of individual companies involved. Acquisition can be said to be less attractive as it result in loss of identity of the acquired. Also the findings concludes that creation of economies of scale, need to gain a higher bargaining power, and business expansions are the main reasons as to why companies conduct M & A. The study also concludes that despite the process of M & A being smooth and the management orientation remaining the same, still uncertainty and confusion among the employees persist. The study further concludes that for effective M & A companies normally have similar approach to rewards and promotions.

Palia's (1993) findings that equity of both the two firms conducting merger and acquisition changes positively thus affecting their economies of scale and bargaining power, which consequently leads to business expansion is in line with the findings that mergers and acquisition in Kenyan oil companies are driven by the need to create economies of scale, gain a higher bargaining power and business expansions. The study further conclude that merger and acquisition would lead to a high positive performance ($p = 0.02$).

Based on the findings the study recommends that there is need for companies to merge to enhance creation of economies of scale, a higher bargaining power, and business expansions. The employees being an important element in offering the human resources should be accorded top priority during mergers and acquisition through regular updates of the merger and the implications of the merger process in order to avoid uncertainties' and confusion among the employees.

The study further recommends that for effective M & A companies should have similar approach to rewards and promotions.

5.4 LIMITATIONS OF THE STUDY

The Time frame of the study was not specific and thus it was done over a mixed period of time. For example one of the companies considered i.e. Total Kenya Ltd had acquired Chevron in

2009 which means that the effects observed may have been different if the merger had been observed over a long duration of time. On the other hand a company like Shell BP had undergone merger in 2006 thus presenting a different scenario.

The oil industry as experienced few mergers and acquisition due to the nature of the industry thus limiting the data collected. The oil industry in Kenya is dominated by a few multinational companies that controls a big percentage of market leaving the other part to the small local players .The limited number of merger and acquisition that have occurred in the oil industry means that there is no variety of data collected which may make the finding different in case of more mergers and acquisition.

The study took on a causal research design which was to determine the relationship between merger/acquisition and financial performance. It is difficult to isolate the effects of merger and acquisition from other external forces that could have contributed to the changes in financial performance. These forces such as fluctuation of crude oil prices, exchange rates gain/loss government policy and other factors could have lend to the changes rather than the variable being tested.

The data collection method used was tedious, time wasting and costly as the questionnaires had to be dropped and picked with respondents not keeping the agreement thus necessitating repeated visits. Also it's not easy to control the questionnaire filing process and this compromises the quality of the data received hence the results.

The use of regression model made the analysis complex due to interdependence of variables involved. Also the estimation error may be within the expected limit or unreasonable depending on the information used. The model therefore can be subjective depending on researcher.

The use of primary data collected through self administered drop and pick questionnaires randomly distributed to management staff of Oil Company may have lend to data collected being a mixture of facts and opinions.

5.5 SUGGESTIONS FOR FURTHER RESEARCH

The research should be conducted over a time frame of between 1-5 years 0-2 years and other duration of time in order to enhance the clarity of the results observed.

Since the study considered the effects of mergers and acquisitions (M & A) on financial performance of oil companies in Kenya, the study should be done across the board for all the companies listed in Nairobi Stock Exchange (NSE) that have experienced mergers and acquisition. This is because different organizations have unique characteristics and diverse contextual realities that might affect M & A. This would bring out a comprehensive empirical results/findings on the determination of effects of mergers and acquisitions (M & A) on financial performance.

The study should be conducted using different research design in order to offer different approach towards the same problem thus enhancing the clarity of the findings by eliminating the influence of other forces affecting financial performance.

To cut on time and the costs spend and to make it less tedious I suggest the research to be done through telephone interview or any other suitable method that can improve the quality of the data through respondents' control.

The study should incorporate analyses of various variables independently to avoid complexity that limits the clarity of results when all are lumped together.

The study should focus primarily on secondary data to eliminate the possibility of personal opinion as a result of collection of data through questionnaires and interview method.

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APPENDICES

Appendix I: Introduction Letter

To Whom it May Concern,

Dear Respondent,

RE: REQUEST FOR DATA COLLECTION

I am a postgraduate student at the University of Nairobi, School of Business, pursuing a Master's degree in Business Administration (MBA). As a requisite to the full completion of the same, I am undertaking a research project on *Effects of Merger and Acquisition on Performance: Case of Kenya Oil Industry*.

You have been selected for data collection being that your company had done mergers or acquisition hence you would be in a good position enabling the study achieves at its objectives. My supervisor and I request you to take a few minutes to respond to the questionnaire attached here-in. Your responses will be kept confidential and the data collected used entirely for education purposes. Your assistance will be highly appreciated.

Yours faithfully,

Johnson K. Ileri

MBA Student

Mrs. W. Nyamute

Project Supervisor

Appendix II: Questionnaire

Tick as appropriate

1. Name of the Company.....

Male () Female ()

2. For how long have you been working for the company?

1-5 years ()

6-10 years ()

11-15 years ()

16-20 years ()

Over 20 years ()

3. Please tick level of management:

i) Lower level management ()

ii) Middle level ()

iii) Senior management ()

4. What was the nature of the corporate action (merger or acquisition)?

Merger (both combined) ()

Acquisition ()

a) If you joined the company before the merger and in case of acquisition, which company did you work for?

(i) The acquiring company ()

(ii) The acquired company ()

iii) Not applicable ()

5. In your opinion, how true are these statements in regard to mergers? If there are some which you consider true but which have not been included, please write them in the space provided for others.

- i) Merger and acquisition (M&A) occurred to create monopolies and fight competition ()
- ii) Merger & acquisition was driven by need for business expansions ()
- iii) M&A was driven by globalisation ()
- iv) The companies conducted M&A to create economies of scale ()
- v) The companies conducted M&A to create more efficiency ()
- vi) The companies conducted M&A to create quality of service ()
- vii) The companies conducted M&A to deploy idle resources ()
- viii) Employees were given top priority during mergers ()
- ix) The companies profitability increased upon a merger ()
- x) Merger or acquisition was driven by cost project to be undertaken ()
- xi) M&A was driven by need to gain a higher bargaining power ()

Any others reason:

.....

.....

.....

.....

6. During the merger of the company you work for:

- i) I received adequate information on what was going to happen ()

- ii) I clearly understood the implications of the merger process ()
- iii) I received regular updates on what was happening ()
- iv) As far as I am concerned, the process was smooth ()
- v) I felt uncertain and confused ()
- vi) I experienced no difference on my work ()
- vii) The values of the organization remained the same ()
- viii) Work procedures and processes remained the same ()
- ix) Behavioural tendencies have remained the same ()
- x) Management orientation remained the same ()

7. How true are the following statements about the merger or acquisition of the company you work for?

- | | Yes | No |
|--|-----|-----|
| i) Both companies had similar approach to rewards | () | () |
| ii) Both companies had similar approach to recruitments | () | () |
| iii) Both companies had similar approach to promotions | () | () |
| iv) Both companies had similar decision making processes | () | () |

THANK YOU

Table 3: Duration working at the company

| | Frequency | Percentage |
|---------------|------------------|-------------------|
| 1-5 years | 10 | 33.3 |
| 6-10 years | 12 | 40.0 |
| 11-15 years | 7 | 23.3 |
| 16-20 years | 1 | 3.4 |
| Over 20 years | 0 | 0 |
| Total | 30 | 100.0 |

Table 4: Mergers and Acquisition (M&A)

| | Strongly Agree | Agree | Neutral | Disagree | Strongly Disagree | Mean | STDEV |
|--|-----------------------|--------------|----------------|-----------------|--------------------------|-------------|--------------|
| Mergers and acquisition(M&A) occurred to create monopolies and fight competition | 4 | 12 | 13 | 1 | 0 | 3.63 | 0.752 |
| M&A was driven by need for business expansions | 17 | 13 | 0 | 0 | 0 | 4.57 | 0.496 |
| M&A was driven by globalization | 8 | 16 | 6 | 0 | 0 | 4.07 | 0.680 |
| The companies created M&A to create economies of scale | 18 | 12 | 0 | 0 | 0 | 4.60 | 0.490 |
| The companies conducted M&A to create more efficiency | 5 | 15 | 9 | 1 | 0 | 3.80 | 0.748 |
| The companies conducted the M&A to create quality of service | 6 | 18 | 6 | 0 | 0 | 4.00 | 0.632 |
| The companies conducted M&A to deploy idle resources | 0 | 8 | 13 | 9 | 0 | 2.97 | 0.752 |
| Employees were given top priority during mergers | 0 | 3 | 17 | 9 | 1 | 2.73 | 0.680 |
| The company's profitability increased upon a merger | 12 | 13 | 5 | 0 | 0 | 4.23 | 0.716 |
| M&A was driven by cost project to be undertaken | 11 | 11 | 5 | 3 | 0 | 4.00 | 0.966 |

| | | | | | | | |
|--|----|----|---|---|---|------|-------|
| M&A was driven by need to gain a higher bargaining power | 18 | 12 | 0 | 0 | 0 | 4.60 | 0.490 |
|--|----|----|---|---|---|------|-------|

Table 5: Respondent Opinion about M & A

| | NO | yes | Mean | STDEV |
|---|-----------|------------|-------------|--------------|
| I received adequate information on what was going to happen | 20 | 10 | 1.333 | 0.471 |
| I clearly understood the implications of the merger process | 23 | 7 | 1.233 | 0.423 |
| I received regular updates on what was happening | 21 | 9 | 1.300 | 0.458 |
| I felt uncertain and confused | 7 | 23 | 1.767 | 0.423 |
| As far as I am concerned, the process is smooth | 3 | 27 | 1.900 | 0.300 |
| I experienced no difference on my work | 12 | 18 | 1.600 | 0.490 |
| The values of the organization remained the same | 13 | 17 | 1.567 | 0.496 |
| Work procedures and processes remained the same | 15 | 15 | 1.500 | 0.500 |
| Behavioural tendencies have remained the same | 11 | 19 | 1.633 | 0.482 |
| Management orientation remained the same | 10 | 20 | 1.667 | 0.471 |

Table 6: Relevance of statement to M & A.

| | NO | yes | Mean | STDEV |
|---|-----------|------------|-------------|--------------|
| Both companies had similar approach to rewards | 3 | 27 | 1.900 | 0.300 |
| Both companies had similar approach to recruitments | 8 | 22 | 1.733 | 0.442 |
| Both companies had similar approach to promotions | 7 | 23 | 1.767 | 0.423 |

| | | | | |
|--|----|----|-------|-------|
| Both companies had similar decision making process | 17 | 13 | 1.433 | 0.496 |
|--|----|----|-------|-------|