

**EFFECTS OF PERFORMANCE ON DIVESTITURE
STRATEGY IN THE KENYAN OIL INDUSTRY**

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DECLARATION

I hereby declare that this research project is my original work and has not been presented for a degree in any other university.

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

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DEDICATION

This project is dedicated first and foremost to the almighty God whose providence, grace and care I cherish.

To my nephews Hesbon Njuguna, Ryan Macharia, Ray Ngoche and niece Lisa Njeri, in addition to my unborn children. I know you will do exploits in your time!

ABSTRACT

In recent years a substantial wave of divestments has occurred in the Kenyan oil industry although this phenomenon has not been sufficiently investigated up to now. The purpose of this study was to extend the current understanding of business divestiture by investigating effects of performance on divestiture strategy and the relationship between divestiture strategy and firm performance. A descriptive census survey was carried out amongst twelve managers from the five major oil companies that have divested from the Kenyan market and the energy regulatory commission.

Findings from the study indicate that firm financial performance is the strongest predictor of divestiture because of dwindling return on investment, low profit margins and high working capital requirements due to upfront payment of duties and compliance to safety standards. Key factors affecting the oil industry and contributing to a great extent to the declining performance include; poor petroleum infrastructure at KPC that contributes to supply constraints and the inefficiencies of KPRL. Lack of appreciation of safety standards, this is further aggrieved by the lack of enforcement of government policy on safety standards. Uneven competition due to lack of a level playing field by the stakeholders in the petroleum sector has significantly contributed to the decline in performance. However, the findings support the fact that divestiture is an instrument for improving firm performance but should be applied as a last resort.

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LIST OF ABBREVIATIONS AND ACRONYMS

B2B	Business to Business
B2C	Business to Customer
BP	British Petroleum
ERC	Energy Regulatory Commission
FTC	Federal Trade Commission
KPRL	Kenya Petroleum Refineries Limited
KPC	Kenya Pipeline Company
LE	Large extent
LPG	Liquefied Petroleum Gas
ME	Moderate extent
PIMS	Product Impact Market Studies
SE	Small extent

CHAPTER ONE: INTRODUCTION

1.1 Background of the study

1.1.1 Divestiture Strategy

Divestiture is broadly defined as sale of assets, or ‘sell offs’, management buyouts of divisions, equity “carve-outs” and spin offs. These divestitures are carried out within the context of portfolio restructuring (Bowman & Singh, 1993), not financial or capital restructuring. “Downscoping” (Hoskisson & Hitt, 1994) is a term recently coined to describe programs of strategic divestiture. Business divestiture means that a firm disposes a significant part of its assets, i.e. in diversified firms, whole business units or divisions (Duhaime & Grant, 1984; Burgelman, 1996) in terms of, e.g. sell-off or dissolution (Chang & Sing, 1999; Mitchell 1994)

Even a shrewd corporate diversification strategy can result in the acquisition of business units that down the road just do not work out. Misfits or partial fits cannot be completely avoided because it is impossible to predict precisely how getting into a new line of business will actually work out. In addition, long-term industry attractiveness changes with the times, what was once a good diversification move into an attractive industry may later turn sour. Reduced performance by some business units is bound to occur, thereby raising questions of whether to keep them or divest them.

A useful guide to determine if and when to divest a subsidiary are to ask the question, “If we were not in this business today, would we want to get into it now?” When the answer

is no or probably not, divestiture must be considered. Divestiture can take two forms: The parent can spin off a business as a financially and managerially independent company in which the parent may or may not retain partial ownership. Or the parent may sell the unit outright, in which case a buyer needs to be found. (Thompson and Strickland)

Divestitures arose as instruments for returning firms to 'optimal levels of diversification' (Markides, 1992, 1995; Williams, Paez, and Sanders, 1988). By using divestitures to reduce diversification, firms could lower their costs of managing business units, reconfigure internal governance structures to raise efficiency, transfer assets to more highly valued uses, have a clearer and more tightly bound group of businesses units, and better protect managerial employment risks over time. The mirror image of an acquisition is divestment. A whole new set of reasons are employed when an owner feels the need to divest; it's a 'sellers market' and the perception is that it won't get any better if the owner waits; relatively substantial capital reinvestment is required to survive or to achieve the next vision for the business.

If an organization with a weak competitive position in an industry is unable to pull itself up by its bootstraps or to find a customer to which it can become a captive company it may have no chance but to sell out. The sell out strategy makes sense if management can still obtain a good price for its shareholders and the employees can keep their jobs by selling the entire company to another firm. The hope is that another company will have the necessary resources and determination to return the company to profitability. If the

corporation has multiple business lines and it chooses to sell off a division with low growth potential, this is called divestment. (Wheelen and Hunger, 2008)

Divestiture strategy is an option when weaknesses in a business are a major obstruction to success in the industry and the costs of overcoming them are unaffordable or are not justified by a cost-benefit analysis, then eliminating the business must be considered. Divestiture offers the best possibility for recouping the firms' investment. (Pearce and Robinson) In deciding whether to divest a business unit, strategists use a number of evaluating criteria: industry's attractiveness, competitive strength, strategic fit with other businesses, performance potential and compatibility with corporate priorities, capital requirements and value to the overall portfolio.

For a diversified company to be a strong performer, a substantial portion of its revenues and profits must come from business units in attractive industries. It is particularly important that core businesses be in industries with a good outlook for growth and above-average profitability. Industry attractiveness is judged from the perspective of the attractiveness of each industry represented in the portfolio, each industry's attractiveness relative to the others and the attractiveness of all the industries as a group. Businesses in the least attractive industries may be divestiture candidates unless they are positioned strongly enough to overcome the adverse industry environment or they are a critical component of the portfolio.

A businesses strategic fit with the other businesses is looked at from two angles; whether the business unit has valuable strategic fit with other businesses the firm has diversified into or has an opportunity to diversify into and whether the business unit meshes well

with corporate strategy or adds a beneficial dimension to the corporate portfolio. A business is more attractive strategically when it has cost-sharing or skill transfer opportunities that can be translated into stronger competitive advantage and when it fits in with the firm's strategic direction. A business is more valuable financially when it can contribute heavily to corporate performance objectives (sales growth, above-average return on investment) and materially enhance the company's overall worth. Just as businesses with poor profit prospects ought to become divestiture candidates so should businesses that don't fit strategically into the company's overall business picture. Firms that emphasize related diversification probably should divest businesses with little or no strategic fit unless such businesses are unusually good financial performers.

An appraisal of each business unit's strength and competitive position in its industry helps corporate managers judge a business unit's chances for success in its industry. Evaluating which businesses in the portfolio enjoy "strong" "average" or "weak" competitive positions adds further rationale for corporate resource allocation. The most likely candidates for divestiture are businesses in a weak competitive position. Many diversified companies concentrate their resources on industries where they can be strong market contenders and divest businesses that are not good candidates for becoming leaders. Corporate manager's strategic making task is to steer resources out of low-opportunity areas into high-opportunity areas. Divesting marginal businesses serves this purpose by freeing unproductive assets for redeployment.

1.1.2 Organizational Performance

The most important considerations in judging business-unit performance are sales growth, profit growth, contribution to company earnings, and the return on capital invested in the business; sometimes, cash flow generation is a big consideration, especially for cash cows or businesses with potential for harvesting. Information on a business's past performance can be gleaned from financial records. While past performance doesn't necessarily predict future performance, it does signal which businesses have been strong performers and which have not.

Industry attractiveness / business strength evaluations should provide a solid basis for judging future prospects. The growth and profit outlook for the company's core businesses generally determines whether the portfolio as a whole will turn in a strong or weak performance. Non-core businesses with sub par track records and little expectation for improvement are logical candidates for divestiture. Business subsidiaries with the brightest profit and growth prospects should have priority for having their capital investments requests funded.

The performance of companies in the modern business-operating environment can be judged using various parameters. The ultimate goal of a firm employing various competitive strategies is to gain an edge over its competitors hence improve performance. Performance is judged using financial and non-financial or behavioural parameters. Johnson Scholes & Whittington (2005) describe firm performance based on key success factors. Financial factors include state of the firm equipment or facilities. Return on capital employed, production and operations costs, prices or rates of produce released to

the market, volume of operations or sales i.e., market share, financial cash flow, technology, profitability and research and development. Behavioural parameters include management style, human resources, product quality, service quality, customer care, firm's image or reputation, marketing effectiveness, technological status, location and processes or systems.

In the past firm performance was generally judged using financial parameters only. However, it has become increasingly evident that the human resources and management factors are key drivers and contribute greatly to overall financial performance. Public image and responsibility to the society have also increasingly become critical factors to overall firm performance.

Companies use various yardsticks for measuring and reporting performance. The two main terms used to measure performance are the firms market share within the particular industry in which it operates and its profitability. Profitability is then used to measure the company return on capital employed hence value to its shareholders. Accountants and economist have derived and used various financial ratios to assess company financial performance. These ratios mainly involve the company liquidity ratio, debt management – financial leverage index, asset management – return on total assets, profitability – cash flow margin and finally return on investment – dividend yield. (Brealey Myers, 2003).

Kaplan and Norton (2001) introduced the balanced scorecard as a more realistic measure of performance. The balance scorecard defines a strategy's cause and effect relationship and provides a framework to organizing strategic objectives into the financial perspective in line with the vision and mission. Key items linked are financials, customer service and

satisfaction index, learning and growths within the organization and internal business processes, internal business process is the path to achieving strong financial results and superior customer satisfaction.

Pearce and Robinson (2007) highlight three economic goals, which define a company's performance guided by strategic direction. These goals are survival in the market, growth and profitability. A firm's growth is tied inexplicitly to its survival and profitability. Survival means a long-term strategy to remain in business and inability to do so mean the company is not capable of satisfying the stakeholders' aims. Although product impact market studies (PIMS) have shown that growth in, other important forms of growth do exist. Growth in the number of markets served, in the variety of products offered, in the technologies that are used to provide goods or services frequently leads to improvements in a firms' competitive ability. Growth means change, and proactive change is essential in a dynamic business environment. Profitability is the main goal of a business organization. No matter how profit is measured or defined, profit over the long term is the clearest indication of a firm's ability to satisfy the principal claims and desires of employees and stockholders. Decisions must be based on the long-term as short-term may produce misleading profit results which overlook the enduring concerns of customers, suppliers, creditors, ecologists and regulatory agents.

According to Eric M. Olson (2002) many managers nowadays adopt a balanced scorecard approach to measuring performance. This position is true for all industries and the most successful firms emphasize the measures and perspectives e.g. customer satisfaction index, internal business processes, innovation and profitability.

1.1.3 The Oil Industry in Kenya

The History of the Oil Industry can be traced to Pennsylvania, USA with the establishment of the Standard Oil Company by John D Rockefeller in 1870 whose key business was the refining, distribution, and transportation of oil throughout America. In Kenya, the first Multinational oil company, Shell is thought to have started its operations in 1900 with its establishment at the port town of Mombasa. Kenya Shell started off as a kerosene and petrol distributor (Ndolo, 2008).

The oil industry has three levels: Upstream, Midstream, and Downstream levels which encompass the main segments in the supply chain. The Upstream level involves the exploration, and production of crude oil; it ends at the point where the crude product is delivered to an export terminal in the country of production. Midstream level includes the transportation and trading of crude oil to refineries. The Downstream level refers to the refining of crude oil into finished products, the storage of crude oil, and the distribution and marketing of finished products to retail service stations or to commercial customers' site. The oil industry in Kenya is basically at the downstream level (Munyao, 2008).

There are three major distinct players in the oil industry in Kenya. Kenya Petroleum Refineries Ltd (KPRL) who are involved in the refining business. Kenya Pipeline Company (KPC) who undertakes the storage and transportation of petroleum products from their Mombasa terminal to the various depots within the country. (Mumo, 2006) The government through the Ministry of Energy lays down the policy guidelines. The Energy Act has established an Energy Regulatory Commission (ERC) that regulates the importation, exportation, transportation, refining, storage and sale of petroleum products.

The ERC is also charged with the responsibility of ensuring the implementation and observance of the principles of fair competition within the industry (Munyao, 2008).

The oil industry is divided into four major marketing fronts namely retail, commercial, aviation and liquefied petroleum gas (LPG). Retail focuses on marketing products to motorists at filling stations strategically located by the roadside. The Commercial arm of marketing is concerned with selling of fuel products to large consumers mainly in the construction and manufacturing sectors. Aviation business is involved with sale of aviation fuels to airlines. LPG section is involved in sale of liquefied petroleum gas. LPG is marketed in bulk for commercial uses or smaller cylinders for domestic use (Mwangi, 2008). Oil marketers operate in an oligopolistic market structure characterized by strong mutual independence, homogeneous petroleum products and high capital entry requirements (Ndolo, 2008).

The oil industry in Kenya was liberalized in October 1994, whereupon an influx of new entrants into the market was experienced. As of May 2003, the new entrants included international affiliates such as Engen. As at end of 2004 new entrants licensed to import crude oil included locally owned companies such as National Oil, Dalbit, Galana, Global, Hass, and Triton, which has since collapsed. There are estimated 40 oil marketing companies operating in Kenya. The dominant ones, who have a national presence, control more than 80% of the market share. These include Total Kenya with a 27.5% market share, Kenol Kobil 19.4%, Shell Kenya 16.1%, Libya Oil 11.7%, Gapco 6.3%, National Oil 4.1%, Hashi Energy 2.2%, Galana Oil 1.8% (PIEA, Petroleum Insight Magazine January – June 2010)

1.2 Statement of the problem

The oil industry landscape in Kenya is dynamic with rapid withdrawals and entry by smaller local operators. In October 2000, Agip sold its local interests to Shell Kenya. In a press release on 9th October 2006, Exxon Mobil, the parent company of Mobil Oil made known its strategic decision to exit the Kenyan market, it sold its local interest to Tamoil Kenya Ltd, the parent company of Libya Oil Kenya Ltd. In 2007 British Petroleum, BP Africa exited the Kenyan market and sold its shares to Kenya Shell. In 2008, Chevron announced its intentions to exit Kenya and other East and Southern African markets, it sold its local interest to Total Marketing. In April 2010, Shell announced its intention to exit Kenya and other nineteen African Markets. Why the exit of these multinational oil companies from the Kenyan market?

The majors in the oil Industry in Kenya are today faced with the proliferation of new entrants, the independent oil companies, most of who are known more for their unethical push for profits than observing business rubrics. This has resulted to increased competition and has consequently lowered the performance of companies in oil industry. The Multinationals cite falling margins and uneven playing field as occasioning their divestment. Moreover, oil marketing and distribution is no longer a lucrative business because demand has outstripped supply. Several Kenyan oil marketers have made a conscious decision to divest their downstream business and concentrate their efforts in the upstream and profitable downstream markets.

Petroleum is a major source of commercial energy in the country, accounting for about 80% of the commercial energy requirements. In spite of the important role played by the large oil companies exiting the country, not much seems to have been done to date. For instance a study by Kinuu (2007) on management of strategic change at Tamoil Kenya, found that organization change at Tamoil was characterized by a lack of clarity on the future state of the organization, an overemphasis on changes to structures, simultaneous introduction of relatively many change programs and mild resistance. Similar to this study is the fact that change management can come in form of divestment. Munyao (2008) in his study on the application of Value Chain in developing competitive advantage at Kenya Petroleum Refineries Ltd described the systems, processes and structures that support value chain in terms of both primary and support activities at KPRL. Moreover, significant value is lost or not enhanced by operations and technology related activities.

Another study by Mwangi (2008) on the relationship between competitive strategies and performance of independent oil companies in Kenya, recommended that independent oil companies set out medium and longer term competitive strategies more in line with the established major oil companies and that they should consistently adopt competitive strategies to improve performance. However, these studies have failed to demonstrate the effects of performance on divestiture strategy, the relationship between performance and divestiture strategy therefore, the purpose of this study is to bridge the existing knowledge gap by finding the effects of performance on divestiture strategy in the Kenyan Oil Industry.

1.3 Objective of the study

The main objectives of the study were

1. To determine the effects of performance on divestiture strategy.
2. To find the relationship between divestiture strategy and performance.

1.4 Significance of the study

This study will be of importance to corporate managers, it will assist them in making sound and informed strategic management decisions. Players in the oil industry in Kenya will gain from the findings of the study by learning from the success and failure stories of firms that have undertaken divestment strategy. Future researchers and Scholars will also gain from the study through increased body of knowledge and literature in the field of strategic management.

CHAPTER TWO: LITERATURE REVIEW

2.1 The concept of strategy

Strategy is the way by which a firm fulfills its mission and attains its objectives. According to Brandenburger & Stuart, the essence of strategy lies in creating favorable asymmetries between a firm and its rivals. According to Barney (1997), Strategy is a pattern of resource allocation that enables firms to maintain or improve their performances. A good strategy neutralizes threats, exploits opportunities, capitalizes on strengths and/or fixes weaknesses. Johnson and Scholes (1997) define strategy as follows: "Strategy is the direction and scope of an organization over the long-term: which achieves advantage for the organization through its configuration of resources within a challenging environment, to meet the needs of markets and to fulfill stakeholder expectations".

2.2 Divestiture strategy

According to the Encyclopedia of Management (2010), divestiture, also known, as divestment, is the release, rather than the acquisition, of assets. Assets can be divested slowly over time, or in a chunk, depending on which strategy works better for the company or institution doing the divesting. Divestiture principally entails restructuring moves of multi-business firms expressed in sale of companies or of their secondary business units. Divestiture is often related to the dismantling of an ownership position because it leads to a total or partial sell off of corporate equity. Hence, the divested firm continues to operate under new ownership and governance structure (Mata and Portugal,

(2000), Hennart et al (1998) and Mata and Portugal (2000) Divestiture may be related to the dismantling of assets, especially in the context of the reorganization of highly geographically diversified corporations (e.g., Owen and Yawson, 2006) or multi-business company groups (e.g., Chang and Singh, 1999). Under this point of view, this strategy leads to the abandonment of some divisions, product lines, business units or activities, as well as autonomization of affiliates abroad.

There are two lines of thought on the divestment activity of restructuring firms. The first rationale suggests that governance structures, including boards of directors, ownership, and managerial incentives, were inadequate to prevent high product diversification because managers have an incentive to increase firm size to increase compensation and governance mechanisms may not adequately constrain them, hence excessive diversification may result (Bethel & Liebeskind, 1993; Gibbs, 1993; Jensen, 1986).

Another rationale is that top executives have made significant strategic errors by pursuing unrelated diversification or by pursuing too many avenues of related diversification simultaneously (Shleifer & Vishny, 1991). Such high relative product diversification may result in poor strategy formulation in other areas, for instance, poor technology strategy, in which Research & Development expenditures are low compared to competitors'. Poor strategy formulation results from loss of strategic control as diversification expands. Strategic control loss and poor strategy can lead to performance difficulties and therefore, restructuring and increased divestiture activities occur to correct the performance problem. Over diversification is defined here as product diversification beyond the level optimal for shareholders (Markides, 1992a, 1992b).

2.2.1 Reasons for Divestiture Strategy

Divestment strategy constitutes a basic element of business policy of a company and is commonly the consequence of a growth strategy. Divestment is not usually the first choice of strategy for a business. However, as product demand changes and firms alter their strategies, there will almost always be some portion of the business that is not performing to management's expectations. Such an operation is a prime target for divestment and may well leave the company in a stronger competitive position if it is divested. The reasons to divest a business are wide-ranging, from short-term cash generation to a desire to restructure the business portfolio by spinning off non-core or low-performing assets. Many international corporations divest some of their operations in order to become more effective and more competitive (Thompson and Strickland, 1992).

The most common reason for a divestiture is a financial one. If a company is breaking itself up through a divestiture, it may be because the divested asset is worth more as a separate entity, or because divesting allows the company to redirect its focus to a primary market. This type of divestiture is undertaken with the consent of stockholders, and if a large company is splitting itself, it can have a profound impact on the market. A company or institution may also choose to divest assets, which are not performing well before they drag the overall investment portfolio down (Thompson and Strickland, 1992). Legal pressures may force firms to divest their operations to avoid penalties for restraint of trade.

Sometimes, divestiture is carried out in response to a government mandate. Many governments are concerned about the growth of monopolies, and if a company acquires too many companies, which are similar to it, it may be ordered to divest to encourage healthy competition. This is most common when a company wishes to acquire another asset. In the United States, the Federal Trade Commission (FTC) determines whether a company should be required to divest or not. The most famous instance of state mandated divestiture in the United States was the 1984 breakup of the Bell telecommunications group, which formerly controlled the majority of telecommunications in the United States. Divestiture may also be related to political pressures: several companies, which do business with oppressive foreign regimes, for example, have divested to improve their public image.

Companies may also opt for divestiture in response to social pressures. Socially conscious investors may be reluctant to invest in companies, which produce certain products, so companies may choose to shut down production of these products in a divestiture in order to attract investors. In the 1980s, many humanitarian organizations encouraged companies to divest from South Africa, as part of the fight against apartheid. Universities and other public institutions are often encouraged to divest from controversial assets, both to separate themselves from questionable governments and to send a message to the companies and other governments, which do business in or with those nations. Extensive divestiture from South Africa may have contributed to the eventual downfall of apartheid, and this wielding of economic power has encouraged other humanitarian organizations to encourage divestiture from nations like Sudan and other human rights violators.

One of the most common motivations for divestiture is economic. Simply put, when an asset is no longer making money for its parent company, the company may choose to sell or otherwise dispose of it before it becomes a liability. Likewise, companies may spin off divisions, which would be more profitable on their own, or be encouraged to sell divisions and assets, which are more valuable to potential buyers than they are to the company. Strong international competition has put more pressure on corporations to rationalize their business scope and to divest non-core activities (e.g., Duhaime and Grant, 1984, Li, 1995; Markides, 1995; Haynes et al, 2003; Nicolai and Thomas, 2006), as well as to relocate manufacturing plants from one production site to another (e.g., Kogut and Kulatilaka, 1994; Pennings and Sleuwaegen, 2000, Belderbos, 2003; Georgopoulos and Preusse, 2006).

Firms may divest when their market share is too small for them to be competitive or when the market is too small to provide the expected rates of return. Firms may also decide to divest because they see better investment opportunities. Organizations have limited resources; they are often able to divert resources from a marginally profitable line of business to one where the same resources can be used to achieve a greater rate of return. Need for increased investment; firms sometimes reach a point where continuing to maintain an operation is going to require large investments in equipment, advertising, research and development, to remain viable. Rather than invest the monetary and management resources, firms may elect to divest that portion of the business. Lack of strategic fit; a common reason for divesting is that the acquired business is not consistent with the image and strategies of the firm. It may also result from decisions to restructure and refocus the existing business (Thompson and Strickland, 1992).

2.2.2 Strategy and Divestment Intensity

Ravenscraft and Scherer (1987) suggested that diversification is a likely antecedent of corporate restructuring resulting from control problems associated with managing diversified operations. Williamson (1985) suggested that the significant increase in tender offers followed firms' widespread adoption of the multidivisional (M-form) structure. Research by Keats and Hitt (1988) suggested that M-form adoption increases diversification. The M-form structure provides an organization apparatus for managing multiple businesses and thereby facilitates acquiring other firms and concomitant increase in diversification.

But as Williamson (1985) noted a "depth-for-breadth" trade-off may occur in an M-form conglomerate. "As the capacity to engage knowledgeably in internal resource allocation becomes strained, problems of misallocation and opportunism intrude" (Williamson, 1985). These problems are likely to result from loss of strategic control and poor strategy formulation as diversification increases. This argument fits with the argument of Ravenscraft and Scherer (1987) who argued that divestiture activity might be related to previous increased acquisition activity. Thus, it may be that divestment activity represents a correction of previous strategic mistakes.

Politics may be involved in divestment activity when restructuring is undertaken. Palmer, Friendland, Jennings, and Powers (1987) and Mahoney (1992) examined the relationship between ownership structures and M-form adoption. Both studies hypothesized that firms dominated by families or financial institutions are less likely than others to adopt M-form structures because families and financial institutions prefer

centralized control of organizations and therefore are reluctant to adopt a structure in which decision control passes to managers. If diversification tips the balance of power to managers, owners may require restructuring divestitures to regain centralized control.

Highly diversified firms have, on the average, invested less in innovation than less diversified firms (Baysinger & Hoskisson, 1989). Hoskisson and Johnson (1992) found that restructuring firms increased their R & D intensity when their diversified scope decreased, perhaps compensation for under funding R & D prior to downscoping. Corporate control of division managers shifts from strategic controls to financial controls to facilitate information processing as diversified business scope increases. At low levels of diversification, under dominant business strategies, where the emphasis is on strategic controls, division managers know that the tactical strategies they implement are understood by corporate managers and evaluated not only on the basis of financial outcomes but also on their strategic applicability. However, once a firm reaches a high level of diversification, employing, for instance, related-linked strategy (Baysinger & Hoskisson, 1989), corporate executives implement financial controls to reduce information processing.

Hoskisson and Johnson (1992) found that Research & Development intensity increases through the manufacturing process, especially if diversified scope is reduced. This relationship suggests that one purpose of restructuring may be to correct competitive deficiencies in the development of new products and processes. Low R & D resulting from high relative product diversification may lead to poor long-term performance. In

fact, Franko (1989) provided evidence that one important contributor to decline in U.S competitiveness in global markets is the “R & D factor” and that restructuring seems to facilitate R & D expenditures. Liebesking and Opler (1993) also found that firms lacking R& D investments were especially likely to restructure. By divesting business units that do not appear central to a firm’s strategy, corporate management may be able to improve its innovative capability.

Hitt, Hoskisson, and Ireland (1990) argued that diversification by acquisition, the dominant process for extending firm scope (Simmonds, 1990), are related to increased debt among diversifying firms. Apparently, use of debt is a frequent financial strategy to fund acquisitions. Hoskisson and Johnson (1992) also found a positive correlation between diversification and debt. Excessive debt, which may create cash flow risk, may lead firms to restructure to reduce debt. Sicherman and Pettway (1992) found that bond (or credit) downgrades significantly reduced sell-off premiums. Thus, there is an incentive for keeping debt at reasonable levels. Doing so may require divestiture to keep down high debt levels. Lee and Cooperman (1989) found that many of the early 1980s restructuring divestitures were attempts to reduce debt levels. This finding suggests that debt affects divestment intensity directly rather than indirectly, through performance.

2.3 Performance and Divestment Intensity

Accounting based performance assesses the past, but market-based performance measures expected future value. Because past performance is a good predictor of future performance, a positive relationship between accounting-based performance and market-based performance is expected. Previous research by Jacobson (1987) and Hoskisson and colleagues (1993) has confirmed this positive relationship. Thus, low relative accounting performance is likely to depress firm market values.

Not only strategy research (Duhaime & Grant, 1984; Montgomery & Thomas, 1988), but also research in finance (Jain, 1985; Sicherman & Pettway, 1987) has shown that poor performance often precedes divestiture of corporate assets. Ravenscraft and Scherer (1987) found that poor and declining profitability often preceded sales of asset. It may be that managers of highly diversified firms lose the vision of potential synergy among business units (Hitt & Ireland, 1986) concluded that “asset sell-offs were primarily inspired by potential gains from focusing on core skills and creating synergy between business units. Duhaime and Grant (1984) and Montgomery and Thomas (1988) also found that divestitures produced performance gains in firms pursuing related diversification, where synergy is emphasized. Thus, firms that are highly diversified relative to their industries and that experience poor performance may restructure to improve synergy and focus on core skills.

Several previous studies have examined the pre-divestiture performance of operating units that were subsequently divested and found that divested units are generally poor performers. Indeed it is now accepted in the literature that a primary motivating factor

for divestiture of an operating unit is the poor performance of the operating unit. Both Vignola (1974) and Ravenscraft and Scherer (1987) find that a downturn in the unit's profitability is the most significant contributor to the profitability of that unit's divestiture. The contention that poorly performing units are likely candidates for divestment is supported in a number of studies (e.g., Duhaime and Grant, 1984; Li and Guisinger, 1991; Hamilton and Chow, 1993; Jagersma and van Gorp, 2003). In particular, most bankruptcies and business dissolutions may stem from low profitability performance, whether the result is poor management or environmental conditions that are changing more rapidly than a business can adapt.

At the corporate level, poor financial performance may also favor divestment (e.g., Hamilton and Chow, 1993; Haynes et al, 2003). For example, in their case study on New Zealand, Hamilton and Chow (1993) report that the necessity of meeting corporate liquidity requirements was among the most important objectives motivating exit. At the international business level, Shaver et. al. (1997) classified the divestitures of their sample as economic unsuccessful because they took place within the short period of five years. According to Kaplan and Weisbach (1992) divestitures that resulted from business failure (e.g., showed losses on sales) were more likely to occur within seven years. Thus, it is expected that divestment of specific assets soon after expansion usually stem from poor performance of the investment given the strong commitment of financial and managerial resources in many foreign direct investment (FDI) projects.

Other studies point out that exit may be due to reasons other than failure and poor performance *per se* (e.g., divestiture policies such as sell-offs, corporate dediversification

strategies). Boddewyn (1979) suggests that the importance of financial factors like poor financial performance should not be overemphasized because many firms divest themselves of affiliates that do not “fit” (strategic dimension) even if they are profitable. Pennings et al (1994) conclude that an undifferentiated position that all divestitures are failures can be erroneous. Belderbos (2003) stresses that not all closures of plants are attributed to business failure. Ghertman (1988) notes that divestment of foreign subsidiaries does not necessarily indicate problems in the subsidiary, nor in the parent company. Rather, it may be due to strategic reorientation of the parent company and to the perception that the subsidiary no longer fits with the parent

On the whole, it should be noted that current accounting-based profitability is not always an indicator of strong performance, if externalities are not accounted for or if short-term profits are attained at the cost of foregone valuable investment or if sequential adaptation strategies of international firms are neglected. Further, measuring the performance of foreign affiliates is difficult because transfer prices are artificially raised or lowered for reasons of tax avoidance and subsidiaries are sometimes constrained in their ability to respond to market incentives due to their subordination to the global strategies of the parent company. On the other, internal subsidiary performance data are confidential and, consequently, are normally difficult to obtain (e.g., Woodcock et al., 1994). Even obtainable, such kind of performance values are frequently hard to interpret because management accounting practices differ between firms and countries, and internal subsidiary performance measures do not have necessarily to conform to legal or accounting standards.

2.4 Approaches to Business Divestment

The phenomenon of international divestment can be theoretically investigated from several viewpoints due to its multiple nature, determinants and characteristics. In an overview of the literature divestment, Chow and Hamilton (1993) identify three streams, that is, industrial organization, corporate strategy and finance. However, none of the existing theories could satisfactorily provide a global explanation of international divestment phenomenon in terms of nature, determinants, exit mode, or decision-making (e.g., Benito, 2005; Shin, 2000; Clark and Wrigley, 1997). Theories of foreign divestment are still in the premature age. Thus, major theoretical gaps still remain.

The first one is industrial organization approach in which literature has been mainly concerned with incentives to exit and impediments to exit (Siegfried and Evans, 1994; Benito, 2005); exit barriers could be also viewed as entry barriers (Caves and Porter, 1976; Clark and Wrigley, 1997). An important incentive to exit is bad performance, which stems from high operating costs, stagnation or permanent decrease in demand, and new aggressive entrants (Siegfried and Evans, 1994). On the other hand, as a substantial impediment to exit can be seen the existence of specific assets which cannot be easily exploited in alternative uses and locations. Specific assets such as durable assets may be significant barriers to exiting (Chow and Hamilton, 1993) it is widely recognized within literature that sunk costs are known as a barrier to international relocation of a firm (e.g., Clark and Wrigley, 1997; Motta and Thisse, 1994; Caves and Porter, 1976).

Moreover, inter-relatedness between units in form of joint production and distribution facilities can also act as barrier to exit (Benito, 2005). Another obstacle to divestment stems from the firm's internal organization, particularly its vertical integration where the upstream unit may compel the continued operation of a downstream unit even if unprofitable because it may contribute positively to the company's overall performance (Chow and Hamilton, 1993). Moreover, international divestment is normally accompanied by lower nationalistic attachment and fewer moral qualms. Hence, the political and social pressure not to close plants may not apply as strongly to foreign managers (Boddeyn, 1983).

The second is Relocation approach, which explains why multinational companies relocate their production activities at global level. It is widely argued that these firms have considerable potential for location flexibility; that is, the ability to switch and re-switch their resources between several host countries taking advantage of national differences in factor endowments, market potentials and economic policies (e.g. Benito, 1997b & 2005; Simoes, 2004 & 2005). To be more precise, Kogut and Kulatilaka (1994) show that operating a multinational network of plants and maintaining the "real option" to vary capacity loadings of different plants in response to relative cost changes is an important competitive advantage of multinational companies.

For instance, international joint ventures are designed as options that are exercised through an acquisition and divestment/ dissolution decisions. These firms have the option to respond to uncertain events (such as change of exchange rates, change of government policies, emergence of new competition, increase of material costs etc.) in

several parts of the world. Consequently, building plants in different countries can generate additional value for the firm by shifting production among them. According to Belderbos (2003), international plant closure due to relocation will occur if the increase in operational profits after relocation exceeds the fixed costs of relocation (the latter consist of fixed investment or adjustment cost in the new plant and the exit costs of the current plant).

Benito (2005) argues that locally-bound subsidiaries based on traditional locational factors such as cost advantages, trade barriers and local tastes, are in general likely to display very high divestment rates. Simoes (2004) shows that international factors (such as international competition patterns and international sourcing policies of companies) rather than local conditions have led to rethinking of both manufacturing locations and the boundaries of the firms themselves.

Thirdly, there is the corporate strategy approach, which contains elements of strategic management and corporate portfolio analysis. Strategic management literature provides valuable insights in the determinants of divestment. The relevant areas include *inter alia* life cycle theory and end-game theory (e.g., Harrigan, 1979; Harrigan and Porter, 1983). Many researchers to the management of particular products, product lines, firms and industries over time have applied the concept of the life cycle. Divestment analysis related to life cycle concept views divestment as one of alternative “endgame strategies” (Harrigan, 1979) for declining industries characterized by stagnation, unexpected poor performance, and uncertainty concerning future returns (Harrigan, 1979; Harrigan and Porter, 1983; Duhaime and Grant, 1984; Benito, 2005). This approach considers a

company destined to move through a number of stages – typically introduction, growth, maturity, and decline- with the divest option coming to the fore in declining industries (Chow and Hamilton, 1993).

Divestment has also been viewed from the corporate portfolio perspective (e.g. Benito, 2005; Hamilton and Chow, 1993; Duhaimé and Grant, 1984), which derives from portfolio management theory. From this point of view, a corporate is considered as a portfolio of assets, products, divisions, business units and activities. A strong interdependency among business of a corporate, particularly of multidivisional or multiproduct firms, may influence its divestment decisions. In this framework where each business unit is in competition with the other businesses for resources, poorly performing units are likely candidates for divestment in form of divestitures or liquidations.

Mata and Portugal (2000), Benito (1997a) and Li (1995) indicate that international diversification entails a higher risk of subsequent exit than foreign ventures within the parent company's main line business. Also, Liebeskind and Opler's (1995) research demonstrates that corporations, which operate in a large number of countries, are far more likely to simplify their corporate structure through divestitures than other companies. Kim (1997) concludes that overseas divestitures result from problems in managing operations.

Finally, there is the financial accounting approach in which, financial studies of divestment have been paying attention to the short-term impact of divestment on

corporate value, i.e. on share prices (e.g., Haynes et al, 2003), and firm performance (Haynes et al, 2002). The organizational capabilities of “over-diversified” companies are inadequate at coping with the range of their activities. Thus, divestment that reverses previous unprofitable or loss-making diversifications should improve the efficiency and performance with which the remaining operations are managed. Bergh (1995) found that diversification lowering divestments improved performance. Gleason et al (2000) observe positive performance gains for the divesting firms related to foreign divested assets in the post-divestment period through the elimination of diseconomies of scale and scope and negative synergies.

There are numerous accounting-based reasons why a corporation might choose to liquidate or sell some part of its business (e.g., Haynes et al, 2003; Haynes et al, 2002; Hamilton and Chow, 1993; Duhaime and Grant, 1984). For example, managers very often make divestment decisions based on the firm’s projected cash flows. Further, no satisfactory profit performance (e.g., Haynes et al, 2002;), pressure from short- and long-term lenders to lighten the debt load of the parent company, and the requirement for more cash (e.g., Hamilton and Cow, 1993) to support higher growth are a few of the more significant ones. Specifically, Hamilton and Chow (1993) found that in the case of New Zealand the divestment decision of large companies was motivated by the need to convert unattractive assets into liquid form. These financially mobile resources could then be held to strengthen the balance sheet or reinvested in either the core business or new activities.

A firm with very many of its products in the growth stage may have insufficient capital to adequately support all of them. Hence, divestment of old products may provide the funds

to properly support the others (Davis, 1974). Cash flow to cover current obligations. Duhaime and Grant (1984) examine three important factors with significant bearings on the decision to divest a) low financial strength (e.g., return on equity) of the divestor firm relative to its industry average; in this case, especially firms' comparisons to their competitors exercise an important influence on their divestment decision. b) Weak performance and prospects of the divested units, and c) low interdependence between the divested unit and the other sectors of the firm's activities.

2.5 Divestment Drivers

These are important firm-specific factors, which may influence the divestment decision.

Ownership entry modes; Our understanding of the international divestment decision-making could benefit greatly from the knowledge concerning market entry and post-entry performance in host countries. It means that the choice among acquisition or Greenfield entrants is related to divestment because these entry forms differ both in expected riskiness and in the importance of coordination and transaction costs. The relevance of transaction cost economics in the divestment context lies primarily in its analysis of the strategic motives underlying choice and change of operation modes. There is considerable supporting evidence that entry modes have different performance levels. This evidence, however, is rather inconclusive. Mata and Portugal (2000), considering two possible ways of exit –i.e., firm closure and capital divestiture–, demonstrate that the entry mode exerts opposite effects on the two modes of exit, that is Greenfield entrants being more likely to shutdown, but less likely to be divested. Overall, they conclude that

Greenfield investments are likely to have a longer lasting presence in the host country than investments by acquisition. On the other, researchers claim that acquisitions are more likely to succeed than new ventures.

Equity ownership; The instability of international joint ventures has been widely recognized in the international business literature (Hennart et al, 1998; Reuer, 2000; Steensma and Lyles, 2000; Pan and Chi, 1999; Dhanaraj and Beamish, 2004). As a consequence of this great instability, many scholars found that fully owned subsidiaries of foreign firms are more likely to survive than joint ventures. Specifically, Pennings et al (1994) found that equally and minority-owned investments are less likely to succeed than fully and majority-owned investments because they involve more risk and conflict potential. Dhanaraj and Beamish (2004) conclude that while foreign investments involving small ownership levels (<20%) show very high mortality rates, those with high ownership levels (>80%) have mortality rates comparable to that of wholly owned affiliates. Mata and Portugal's findings (2000) indicate that ownership arrangements such as majority joint ventures and fully owned affiliates, experience a lower probability of failure than do minority holdings.

Experience; Organizational-learning theory suggests that prior learning facilitates the learning and application of new, related knowledge. In the foreign entry literature, advocates of the Uppsala stage model of internationalization have argued that firms expand slowly from the domestic bases into progressively distant areas. Experiential learning from previous entries is the driving force behind new investments. In other words, entry into a new foreign market requires a learning period over which entering

firms establish themselves. Host country experience can counter location-specific disadvantages to improve a subsidiary's likelihood of survival. Rich evidence concerning the economic success of FDI highlights the importance of country-specific knowledge and industry-specific knowledge within the target country.

Foreignness; Only a few studies appear to have compared the survival of foreign-owned and domestic companies. Empirical evidence in this area is rather inconclusive. According to Kronborg and Thomsen (2006), the relative survival rates of foreign and domestic companies principally depend on a balance of their advantages (e.g., of ownership and internalization) against the liability of foreignness. These authors comparing over the 100-year period 1895-2001 the survival of foreign subsidiaries in Denmark to a control sample matched by industry and firm size found that foreign-owned companies have a higher survival probability, although the foreign survival advantage appears to be eroded by globalization. Li and Guisinger' results show (1991) that foreign-controlled firms fail less often than domestically owned firm. Zaheer and Mosakowski's findings (1997) confirm that there is a liability of foreignness, and that it decreases over time.

Cultural distance; Cultural similarity between the home and the host country should facilitate the implementation of the decision to establish a subsidiary abroad due to easier monitoring and coordination of production activities in the various locations (e.g., Benito, 1997a). On the contrary, the cultural distance of home country from host countries has been identified as a negative factor in the participation of firms in FDI, and, at the same time, has been cited as a positive factor in firms' choice of less committed entry modes.

For instance, cultural distance caused foreign investors to avoid full ownership because distance increases information costs and difficulty in transferring management skills (Barkema et al, 1997). Also, the findings of Li and Guisinger (1991) support their hypothesis that the U.S. affiliates whose foreign parents are from culturally dissimilar countries are more likely to fail than those from culturally similar countries.

Size; Industrial organization post-entry performance literature investigates the relationship between firm size and survival. According to McCloughan and Stone (1998), foreign plant survival is likely to improve with size; by size, it is meant average size of plant or of business over its lifetime and not initial size, or size at the point of entry which was found to be unimportant. Mata and Portugal (2000) investigating closures and divestitures by foreign entrants, conclude that firm size is clearly significant (with the association negative) in the case of closure, but not in the case of divestiture. Also, the same authors (2002) examining the survival of new domestic and foreign-owned firms found that the probability of exit decreases with firm current size.

Diversification; Many international business studies have investigated the relationship between product diversification and the exit hazard of foreign subsidiaries. Their results support the argument that the more remote the business of the new subsidiary from the core product areas of the parent operations, the greater is the uncertainty involved. Thus, an “over diversification” of a firm has important negative implications for the performance and survival of foreign affiliates. In particular, the findings of Li (1995) indicate a higher exit rate for subsidiaries that diversify than for those that stay in the parent’s main product areas. Gibson and Harris’s findings (1996) illustrate that

diversified; multi-plant firms were more likely to close plants. Pennings et al (1994) conclude that international firm expansions were more persistent when related to a firm's core skills. The results of Haynes et al (2003) suggest that the relative extent of divestment is positively related to a firm's level of diversification, whereas the findings of Duhaime and Grant (1984) show that divested units are characterized by low interdependency with other units of a firm. Also, Benito (1997a) found that related (horizontal) subsidiaries are less likely to be divested than unrelated (non horizontal) affiliates.

Financial performance; Deterioration in performance is expected to raise pressure on managers of firms to divest (e.g. Haynes, et al, 2003). In fact, some scholars have identified financial performance such as profitability, liquidity and leverage with significant bearings on the divestment decision. At the profitability level, Hamilton and Chow (1993) provide evidence that the most important divestment factor is the low return achieved in the divested units. This finding is also consistent with that of Duhaime and Grant (1984) who conclude that divested units will be characterized by low financial strength. At the same time, their research results give strong support to the hypothesis that divestment decisions tend to be made when corporate financial strength (as measured by ROE), is low by comparison to industry financial strength. At the liquidity level, Hamilton and Chow (1993) found that typical divestment was motivated by the need of a company to convert unattractive assets into liquid form which is then use *inter alia* to satisfy overall liquidity requirements. At the leverage level, the findings of Haynes et al (2003) indicate that the extent of divestment activity is positively associated with the extent of a firm's debt burden.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This section sets out the research methodology that was adopted to meet the objectives stated in chapter one of this study. The section deals with the methodology that was used in carrying out the study. It is sub divided into the research design, target population, research instruments, instrument validity, instrument reliability, data collection procedures and data analysis techniques.

3.2 Research design

A descriptive census survey was conducted. The design is best for a qualitative study. A descriptive research according to Cooper & Schneider (1999) is used to obtain information concerning the current status of the phenomena, to describe ‘what’ ‘how’ ‘where’ of a phenomenon with respect to variables or conditions in a situation. The methods involved range from the survey, which describes the status quo, the correlation study that investigates the relationship between variables, to developmental studies, which seek to determine changes over time. The research design used was a descriptive census survey. The survey is a non-experimental, descriptive research method. Surveys can be useful when a researcher wants to collect data on phenomena that cannot be directly observed. It has been observed that census study is feasible when the population is small and variable.

3.3 Population of the study

The populations of interest were the major oil marketing companies in Kenya. There are estimated forty oil marketing companies in Kenya. However the study concentrated on the five major oil marketing companies that have undertaken divestiture strategy. The target populations were two managers from each of the five major oil marketing companies and the Energy Regulatory Commission. (Petroleum Institute of East Africa)

3.4 Data Collection

In order to investigate effects of performance on divestiture strategy in the Kenyan oil industry, self-administered drop and pick questionnaires were distributed to two managers in each of the five major oil companies that have undertaken divestment strategy, in addition to two senior officials from the energy regulatory commission. The researcher used semi-structured questionnaires as the main data collection instrument to obtain primary data. The questionnaires had both open and close-ended questions designed to elicit specific responses for qualitative and quantitative analysis respectively. The close-ended questions provided a more structured response to facilitate tangible recommendations. The open-ended questions provided additional information that may not have been captured in the close-ended questions. Secondary data sources were employed through the use of information available in companies' websites and published financial reports to supplement the data received from questionnaires and information obtained from the interviews conducted.

3.5 Data Analysis

The data was analyzed by the use of descriptive statistics to summarize and relate variables, which were attained from the administered questionnaires. The data was classified, tabulated and summarized using means, standard deviation, and frequency distribution. Tables and pie charts were used for presentation of the findings. However, before final analysis was performed, data was cleaned to eliminate discrepancies and thereafter, classified on the basis of similarity and then tabulated. Cross tabulation was used to compare the existence of relationship between divestiture strategy and performance. Nachmias (1996) Statistical package for Social Science (SPSS), enables a researcher to recode variables, to deal with missing values, to sample weight and select cases; to compute new variable and effect permanent or temporary information. Therefore for easy handling of the recurring needs and to ensure efficient and effective computerized data analysis, we shall use the Statistical Package for Social Sciences (SPSS) software.

CHAPTER FOUR: DATA ANALYSIS, FINDINGS AND DISCUSSIONS

4.1 Introduction

This chapter presents the analysis and findings with regard to the research objectives stated in chapter one. The findings are presented in percentages and frequency distributions, mean and standard deviations. A total of 12 questionnaires were issued out to two senior officials at the energy regulatory commission and to two managers amongst the five major oil marketing companies that have been involved in divestment. Of the 12 questionnaires issued, 10 were returned. This represented a response rate of 83.3%. The findings from the study were then analyzed, interpreted and summarized.

4.2 General information

This represents the general information regarding the five major oil marketing companies.

4.2.1 Ownership structure

Firstly, the respondents were requested to indicate the ownership structure of their companies. The results are shown in table 4.1

Table 4.1: Ownership structure

	Frequency	Percent	Cumulative Percent
Foreign	4	80.0	80.0
Partly Local and Partly Foreign	1	20.0	100.0
Total	5	100.0	

As shown in table 4.1, the results indicate that, four of the five major oil marketing companies are foreign owned and one of the major oil marketing companies is partly local and partly foreign owned. There is therefore, an increased tendency by the foreign owned oil marketing companies to exit the Kenyan market compared to the oil marketing companies, which have both local and foreign ownership.

Secondly, the respondents amongst the five major oil marketing companies were requested to give the scope of operations of their oil marketing companies. All the respondents indicated that their scope of operation is global and therefore this is an indication that divestiture strategy is highly likely to occur among companies with a global scope of operation compared to companies with a local scope of operation.

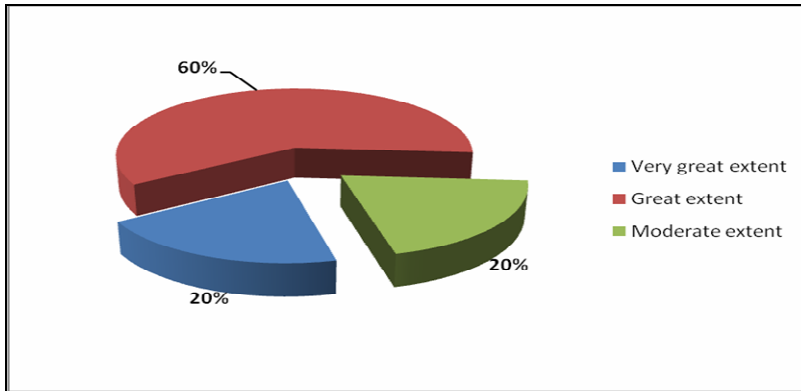
Finally, the respondents were requested to indicate the nature of business that their oil marketing companies are involved in. The results indicate that the five major oil marketing companies that have undertaken divestiture, their nature of business is wide. They are involved in all the business activities characteristic of a downstream market that is retail, business to business (B2B), business to customer (B2C) and Aviation; therefore, divestiture strategy is favourable for a business with a wide variety of business activities compared to dissolution which does not promote continuity of a business entity.

4.3 Performance

4.3.1 Influence of Performance on divestiture strategy

Firstly, the respondents were requested to indicate the extent to which performance influenced divestiture strategy in their oil marketing companies. The results are shown in figure 4.1

Figure 4.1: Performance influence on divestment



As shown in figure 4.1, the results indicate that 60% of the respondents agreed to a great extent with the fact that performance influenced divestiture strategy. 20% of the respondents attested to the fact that performance influenced divestiture strategy both to a very great extent and to a moderate extent. This therefore indicates that the exit of the major oil marketing companies from the Kenyan market has significantly been influenced by performance.

Secondly, the respondents were asked in a five point likert scale, to indicate the extent to which the below listed oil industry factors determined the performance of the major oil marketing companies in Kenya. The results are shown in table 4.2

Table 4.2: Key Industry factors effect on performance

Key Industry factors	Mean	Std. Deviation
i) Petroleum infrastructure (Pipeline and storage)	4.7000	.6749
ii) Safety standards (e.g. double walled tanks)	3.9000	.7379
iii) Competition	3.9000	1.1005
iv) Piracy	2.9000	1.1005
v) New entrants	3.1000	1.1972

The results in table 4.2 above indicate that petroleum infrastructure with a mean and standard deviation of 4.700 and 0.6749 respectively is a significant determinant of performance of the major oil marketing companies. Safety standards with a mean of 3.9 and standard deviation of 0.7379 are the second most significant determinants of performance. The third most significant determinant of performance is Competition with a mean of 3.9 and standard deviation of 1.1005. The results indicate that new entrant with a mean of 3.1 and standard deviation of 1.1972 and Piracy with a mean of 2.9 and standard deviation of 1.1005 do determine performance of the major oil marketing companies in Kenya but less significantly.

Thirdly, the respondents were asked to indicate, how their companies had performed with regards to the below listed performance indicators for the last five years. The range was ‘declining (1)’ to increasing (4). The scores of declining have been taken to present a variable which had mean score less than 1.5. The scores of mixed have been taken to represent a variable with a mean score of 1.6 to 2.5 and the score of increasing have been taken to represent a variable, which had a mean score of above 2.5. A standard deviation of >0.9 implies a significant difference on the impact of the variable among respondents. The results are shown in table 4.3

Table 4.3: Firm performance with regard to performance indicators

Performance Measurement Indicators	Mean	Std. Deviation
i) Market share	2.3000	.97183
ii) Sales growth	2.1000	1.25167
iii) Profitability	1.7000	.48305
iv) Return on investment	1.8000	.91894

The results in table 4.3 above show that the various performance indicators demonstrate a general decline of performance of the major oil marketing companies. Profitability has experienced the most significant decline with a mean of 1.7; second most significant decline is on return on investment with a mean of 1.8, third most significant decline is on the sales growth. Market share has experienced the least significant decline with a mean of 2.3. The variation in the standard deviation is an indication that some of the company's performance varied with regards to the above performance indicators. The declining performance indicators amongst these major oil marketing companies indicate that divestiture of these companies was prompted by their deteriorating firm performance.

4.4 Divestiture Strategy

The respondents were requested to indicate in a five point likert scale, the extent to which they agreed with the below statement on divestiture. The range was 'no extent (1)' to 'very great extent' (5). The scores of no extent/less extent have been taken to present a variable which had mean score of 0 to 2.5 on the continuous Likert scale ;($0 \leq S.E < 2.4$). The scores of 'moderate extent has been taken to represent a variable with a mean score of 2.5 to 3.4 the continuous Likert scale: $2.5 \leq M.E. < 3.4$). The score of both great/very great extent has been taken to represent a variable which had a mean score of 3.5 to 5.0 on a continuous Likert scale; $3.5 \leq L.E. < 5.0$). A standard deviation of >1.1 implies a significant difference on the impact of the variable among respondents. The results are shown in table 4.4

Table 4.4: Level of agreement with the statements on divestiture strategy

Divestiture statements	Mean	Std. Deviation
a) Divestiture is more of a strategic move than as a result of poor performance.	4.3000	.94868
b) Divestiture is a correction of a previous strategic mistake e.g. that of over-diversification.	2.4000	1.26491
c) Divestiture is a favourable option for improving firm performance.	3.6000	1.07497

The results in table 4.4 (a) to the question ‘divestiture is more of a strategic move than as a result of poor performance’, a mean of 4.3 indicates to a great extent that divestiture is a strategic move. This therefore demonstrates that, not all divestments of the major oil marketing companies has been as a result of poor performance, some of the companies have undertaken divestiture as part of its corporate strategy.

The results in table 4.4 (b) to the question ‘divestiture is a correction of a previous strategic mistake e.g. that of over-diversification’, a mean of 2.4 indicates that divestiture is not a correction of a previous strategic mistake. Therefore, these oil marketing companies have not used divestiture strategy to curtail over-diversification of their companies.

The results in table 4.4 (c) to the question, ‘divestiture is a favourable option for improving firm performance’, a mean of 3.6 indicates that divestiture is indeed a favourable option for improving firm performance, therefore these major oil marketing companies have undertaken divestiture strategy largely, in an effort to improve firm performance

Lastly, the respondents were requested to indicate the challenges faced by their oil marketing companies in Kenya that have contributed to the divestment of these companies. The key challenge that significantly determines performance is the supply constraint, which increases costs of oil marketing companies. The constraints include port congestion due to limitation of jetty facilities, storage and pump over capacity especially within the KPC system. Delayed berthing of vessels attracts significant demurrage charges. The Mombasa port cannot accommodate large vessels due to the depth of the channel and therefore economies of scale cannot be achieved through savings in freight charges. The requirement by law to process crude oil within KPRL, which is a hydro skimming refinery with no product enhancement capacity, is another constraint

CHAPTER FIVE: SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The results of this study confirm the fact that, the multinational oil corporations which enjoy a global scope of operation, have mainly been involved in the divestment of their business entity from the Kenyan and African markets at large, so as to concentrate their operations in the more lucrative markets of Europe and Asia. The exit of these multinational oil corporations went ahead despite the fact that they enjoyed economies of scale as a result of their engagement in a wide range of business activities within the oil industry.

The results of this study demonstrate that firm financial and market performance experienced a general decline with regards to sales growth, market share, firm profitability and return on investment. However, the firm's profitability and return on investment declined by a great extent over the last five years and thus prompted the corporate restructuring of the multinational oil corporations with increased focus on the upstream business and reduced focus on the downstream business. The respondents overwhelming supported the fact that divestiture is a favourable option for improving firm performance. There was moderate support for the fact that divestiture strategy is a correction of a previous strategic mistake.

A number of key drivers to this declining performance have been identified. They are volatility of crude oil prices in the international market. The change in taxation policy by

the government in August 2005 where all taxes for petroleum products were to be prepaid at the port of Mombasa increased the cost of inventory financing. These key drivers are further compounded by increased competition, strict credit policy which made the companies an unattractive supplier of petroleum products to many traders. High operational safety standards with regard to road transport and in the depots meant that for instance no truck is driven after nightfall and no truck with tyres whose tread was less than three millimeters deep could access the depot.

5.2 Conclusion

The findings of this study strengthen our understanding of the effects of performance on divestiture strategy and the relationship between divestiture strategy and performance. The findings from the study mainly indicates that firm financial performance is the strongest predictor of divestiture because of dwindling return on investment, low profit margins and high working capital requirements due to upfront payment of duties and compliance to safety standards. Key factors affecting the oil industry and contributing to a great extent to the declining performance include; poor petroleum infrastructure at KPC that contributes to supply constraints and the inefficiencies of KPRL.

Lack of appreciation of safety standards, this is further aggrieved by the lack of enforcement of government policy on safety standards. Uneven competition due to lack of a level playing field by the stakeholders in the petroleum sector has significantly contributed to the decline in performance. The study further suggests that new entrants into the oil industry and the piracy menace experienced along the Gulf of Eden were not

predictors of divestiture. Although the business were generally not loss making, companies prefer more profitable markets with less or none of the above sighted constraints where shareholders wealth would be maximized

Divestiture is a strategic move and would be undertaken as part of corporate strategy. Divestment of the major oil companies from the Kenyan market was prompted by successive failure of several initiatives geared towards increased profitability and meeting shareholders expectations. However, it is recommended that divestiture should be a last resort after several attempts aimed at turning around a firm into a profitable venture have failed to bear fruit. The findings suggest that divestiture plays a very important role in restructuring organizations corporate portfolio to maximize shareholder value, future growth and cash flow.

5.3 Limitation of the study

The limitation of this study is, the credibility of the data collected from the questionnaires is limited to the respondents' truthfulness despite my attempts to verify the data collected.

5.4 Recommendation

5.4.1 Recommendation of the study

This study found that the Kenyan petroleum infrastructure at KPC, KPRL to be the most significant determinant of the performance of the major oil marketing companies in Kenya. Performance of the major oil marketing companies in terms of profitability, return on investment, and sales growth has been on the decline. Supply constraint is the

major challenge facing these oil marketing companies, which is as a result of the poor petroleum infrastructure. Petroleum is a major source of commercial energy in the economy, accounting for about 80% of the commercial energy requirements. It is therefore recommended that the government through the Ministry of Energy develop policy guidelines aimed at expanding and improving efficiency of the petroleum infrastructure in the country both at KPC and KPRL.

5.4.2 Recommendation for further research

Divestment ranges from regions, nations, via industries, to specific firms. Surprisingly not many divestment studies have been conducted in the area of international business. It is recommended that further research be done on divestiture in Kenyan manufacturing firms, in addition to a study on the relationship between divestiture and diversification strategies

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APPENDICES

APPENDIX A: QUESTIONNAIRE

Study on effects of performance on divestiture strategy in the Kenyan oil industry

Please answer the following questions in the spaces provided. The information obtained shall be used in the study only and not for any other purpose.

Section A: General Information

1. Name of your organization?
2. Year of Incorporation?
3. Position held in the organization?.....
4. Ownership Structure?
 - a) Local ()
 - b) Foreign ()
 - c) Partly Local & Partly Foreign ()
5. Scope of Operations?
 - a) Local ()
 - b) Regional ()
 - c) Global ()
6. Nature of Business?
 - a) Retail ()
 - b) Business to Business ()
 - c) Business to Customer ()
 - d) Aviation ()
 - f) All the above ()

Section B: Performance

1. To what extent has organizational performance influenced the divestment of multinational oil corporations' in Kenya?

{5 Very great extent; 4 great extent; 3 moderate extent; 2 less extent; 1 no extent)

.....

2. Between firm performance and corporate strategy which of them has had a stronger influence on the divestment of the major oil companies in Kenya?

.....

3. To what extent do the following key oil industry factors affect performance?

	5	4	3	2	1
	Very great extent	great extent	moderate extent	less extent	no extent
a) Petroleum Infrastructure (Pipeline & storage)	[]	[]	[]	[]	[]
b) Safety standards (e.g. double walled tanks)	[]	[]	[]	[]	[]
c) Competition	[]	[]	[]	[]	[]
d) Piracy	[]	[]	[]	[]	[]
e) New entrants	[]	[]	[]	[]	[]

4. How has your company performed with regards to the following performance measurement indicators for the last 5 years?

	4	3	2	1
	Increasing	Stable	Mixed	Declining
a) Market share	[]	[]	[]	[]
b) Sales growth	[]	[]	[]	[]
c) Profitability	[]	[]	[]	[]
d) Return on investment	[]	[]	[]	[]

Section C: Divestiture Strategy

1. In your opinion what are the main factors that have influenced the divestment of the major companies in the Kenyan oil industry?

.....
.....
.....

2. To what extent do you agree with the below statements on Divestment?

	5	4	3	2	1
	Very great	great	moderate	less	no extent
	extent	extent	extent	extent	
a) Divestiture is more of a strategic move than as a result of poor performance.	[]	[]	[]	[]	[]
b) Divestiture is a correction of a previous strategic mistake that of over- diversification.	[]	[]	[]	[]	[]
c) Divestiture is a favourable option for improving organizational performance.	[]	[]	[]	[]	[]

3. What are the major challenges faced by oil marketers in Kenya?

.....
.....

THANK YOU FOR YOUR COOPERATION

APPENDIX B: OIL MARKETING COMPANIES IN KENYA

MARKET SHARES JANUARY - JUNE 2010

	Company	Market Share %
1	Total Kenya	27.5
2	KenolKobil	19.4
3	Kenya Shell	16.1
4	Libya Oil	11.7
5	Gapco Kenya	6.3
6	National Oil	4.1
7	Hashi Energy	2.2
8	Hashi Petroleum	2
9	Galana Oil	1.8
10	Oilcom	1.5
11	Engen Kenya	1.1
12	Gulf Energy	1.1
13	Rivapet	0.8
14	Fossil	0.8
15	Trojan International	0.7
16	Bakri International	0.4
17	Kamkis	0.3
18	Petro Oil	0.3
19	MGS International	0.3
20	Dalbit International	0.2
21	Muloil	0.2
22	Global Petroleum	0.2
23	Addax Kenya	0.2
24	Intoil	0.2
25	Others e.g Vitol, Metro, Pentoil	0.6
	TOTAL	100

Source: Petroleum Institute of East Africa