

**EFFECT OF MERGER AND ACQUISITION ON THE FINANCIAL PERFORMANCE
OF OIL COMPANIES IN KENYA**

BY

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DECLARATION

This research project is my original work and has never been presented in any other university or college.

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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 research project is dedicated to my family for their love and caring support towards the completion of this project.

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ABSTRACT

The study was carried out with an objective of establishing the effect of merger and acquisition on the financial performance of oil companies in Kenya. The research design adopted was causal research design. The study focused on the mergers and acquisitions that have occurred between year 2003 and 2013 within the industry. The population of this study was the oil companies in Kenya that have merged between 2003 and 2013. Secondary data was used from the financial statements of the companies involved in the merger/acquisition process. A comparison was made between three years pre-merger/acquisition and three years' post-merger/acquisition period using the financial ratios. Analysis of the data acquired was performed through use of the SPSS software (version 16).

Regression analysis was conducted to establish the relationship between financial performance and the independent variables that is the liquidity, solvency, debt to equity ratio, profitability and efficiency of the merged/acquired oil companies in Kenya. The study findings indicate that the goodness of fit model was adequate reported by r squared of 0.553 which means that 55.3% of the variation in financial performance is explained by changes in liquidity, solvency, profitability and efficiency. The correlation coefficient of 74.4% means that the dependent variables have a strong correlation the independent variable. Analysis of the ANOVA results showed that there is a significant joint relationship between financial performance and liquidity, solvency, profitability and efficiency of p-value 0.003 at 5% level of significance. The study concludes that there is decrease of financial performance of oil companies in Kenya following a merger or acquisition process.

The study recommends that the management should not only undertake mergers and acquisitions in order to improve operation and sustain failing businesses but also improve their competitiveness and financial standing. Management should come up with a sound strategy towards asset and liability management so as to avert the problem of mismatching investments and also the quality of assets should be enhanced. Management should put into consideration the degree of transferability and marketability of assets invested in so that these assets can provide liquidity to the firm with ease.

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ABBREVIATIONS

ANOVA	Analysis of Variance
CR	Current ratio
EPS	Earning Per Share
ERC	Energy Regulatory Commission
FTC	Federal Trade Commission
KPC	Kenya Pipeline Company
KPRL	Kenya Petroleum Refinery Limited
M&A	Merger and Acquisition
OMC	Oil Marketing Companies
PE	Price Earning
PIEA	Petroleum Institute of East Africa
ROE	Return on Equity
RTP	Restrictive Trade Practices
SPSS	Statistical Package for Social Sciences

CHAPTER ONE

INTRODUCTION

1.1. Background of the Study

Kemal (2011), in today's globalized economy, mergers and acquisitions (M&A) are being increasingly used the world over for improving competitiveness of companies through gaining greater market share, broadening the portfolio to reduce business risk, for entering new markets and geographies, and capitalizing on economies of scale among other. The motives behind mergers and acquisitions are economy of scale, economy of scope, increase market share and revenues, taxation, synergy, geographical and other diversification.

Krishna and Paul (2007), the firms are motivated for mergers or acquisitions for various reasons with realization that business combinations provide an opportunity to create new economic value for their shareholders. This new value can be created through taking advantage of the economies of scale to be achieved through the combination as a result of the new firm performing a function more effectively more than the two separate firms. The value would also be increased by combining firms with complimentary resources for efficiency and effectiveness in the business operations. Other potential areas of increasing value to shareholder would be in capturing of tax benefits on the merger and acquisition procedure, increasing product markets rates as a result of the small firms turning to be dominant firm in the industry and finally adding value by improving the target company's management.

Merger and acquisition can still be motivated by such classic commercial and economic considerations as broadening the range of related products and the geographic market, diversification, and the risks and benefits of vertical integration. Finally, new or modified tax regimes, the cost of capital, and policy on such things as foreign property, the cost of capital, economic regulations and privatization also have an effect on the inter-sector/international variations in the number of merger and acquisition.

Ruth Bender and Keith Ward (2009) indicated that companies need to grow in order to generate capital gains for their shareholders and to justify the growth value already priced into their

shares. One way of a company growth can be achieved through merger and acquisition process. Accordingly, many companies look to mergers or acquisitions as a means to obtain the appropriate growth within the required time frame.

1.1.1. Merger and Acquisitions

Beena (2011) defines merger as the activity by which two or more companies decide to come together and function as one for achieving strategic objectives or goals like resource sharing, resource utilization, economies of scale achievement or cost minimization or any other operational or financial advantage for both the companies. A merger is the combination of two or more companies, generally by offering the stockholders of one company securities in the acquiring company in exchange for the surrender of their stock where one company or both loose entity.

According to Halpern (1983), mergers occur when an acquiring firm and a target firm(s) agree to combine under legal procedures established in the states in which the merger participants are incorporated. Manne (1965) argued that in a merger, the acquiring concern will be a corporation and not an individual, and the medium of exchange used to buy control will typically be shares of the acquiring company rather than cash. A merger requires the explicit approval of those already in control of the corporation. And most statutes require more than a simple majority vote by shareholders to effectuate a merger.

The term “acquisition” is used to refer to any takeover by one company of the share capital of another in exchange of cash, ordinary shares, or loan stock Halpern (1983). The acquiring firm retains its name and identity, and it acquires all of the assets and liabilities of the acquired firm leading to none existence of the acquired firm. M&As have been popular methods of increasing the size and value of firms in modern times. Compared to the older system of increasing value through organic growth, M & As are faster and in most cases cheaper. The terms M&As have been used interchangeably in this study.

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 M&As

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 (2008), Shell-BP (2006), Total Kenya Ltd – Chevron (Caltex) (2009) acquisition among others (Njoroge, 2008 and PWC, 2010).

1.1.2. Financial Performance

Operating performance studies attempt to identify the sources of gains from mergers and to determine whether the expected gains at announcement are ever actually realized. If mergers truly create value for shareholders, the gains should eventually show up in the firms' cash flows. These studies generally focus on accounting measures of profitability, such as return on assets and operating margins, (Andrade, Mitchell, & Stafford 2001).

Financial performance can be described as a measurement of how well a firm uses its assets from its primary mode of business to generate revenue. It is also used as general measure of a firms overall financial health over a given period of time and can be used to compare industries as sectors in aggregation. According Subramanyam and John (2009), financial performance of a company is measured through financial analysis in the context of the goals and strategy of the company. This can be achieved through usage of two principal tools of the financial analysis that are usually used are the ratio analysis and cash flow analysis.

Ratio analysis of a company's present and past performance provides the foundation of making forecast of future performance. The objective of ratio analysis is to evaluate the effectiveness of the firm's policies in the four levers of management also referred to as the drivers of a firms' profitability and growth that the managers use in order to achieve the growth and profit targets of the company.

Cash flow analysis is the evaluation of how a company is obtaining and deploying its funds. This analysis provides insights into a company's future financing implications. A company that funds new projects from internally generated cash (profits) is likely to achieve better future performance than a company that either borrows heavily to finance its projects or, worse, borrows to meet current losses.

Pandey (2005) defines a cash flow statement as a statement of changes in financial position on cash basis of a firm. It summarizes the causes of changes in cash position between dates of two financial periods. It indicates the sources and uses of cash within the firm.

Cash flow analysis supplements ratio analysis in examining a firm's operating activities, investment management and financial risks. It is used to evaluate on the strength of the firms internal cash flow generation; the ability of the firm to meet its short term financial obligations such as interests rates from its operation; the amount of cash used by the firm in investment and finding out the consistency in investments with regard to the business strategy; how the dividends have been paid, if from internal cash flow or for external financing; types of external financing used by the firm and finally to evaluate the excess cash flow after making capital investment.

1.1.3. Merger and Acquisitions and Financial Performance

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. Bowman and Singh (1999) classified mergers and acquisitions activities into three categories. Financial mergers and acquisitions being one of them, includes changes in the capital structure of a firm, including leverage buyouts, leveraged recapitalization and debt equity swaps. A common way for financial mergers and acquisitions is increasing equity through issuing of new shares.

The operating environment for the oil industry in Kenya remains challenging with numerous challenges before sales of the product to the consumer. These include; payment of taxes in advance before accessing the product, regulation of pump prices in the country, queuing of ships at the port that lead to high value of demurrage charges, pipeline pumping capacity limitation that lead to stock outs in upcountry markets and stiff competition in the industry. The demands by the consumer of having low prices tend to be challenging to the industry which usually lead to low margin enjoyed by the participants.

1.1.4. Oil Companies in Kenya

The oil companies in Kenya also referred to as Oil Marketing Companies (OMCs) in this study represent the firms that are involved in marketing and distribution of petroleum products in Kenya. They comprise of both local and multinational companies. The industry is mainly regulated by Energy Regulatory Commission (ERC).

The oil industry in Kenya is characterized by above 75 oil marketers. It is governed by the Kenyan law which covers operations from crude importation, refining and retailing. It is an oligopolistic structure dominated by about 3 major players. The three players control over half of the market share with 54.9% of the total market share as at March 2014 (Total Kenya controlling 21.7%, Vivo Kenya 18.9% and KenolKobil 13.9%) according to PIEA, (2014). The sector is very competitive characterized by price controls, common non-differentiable products and strict taxation structure within a liberalized economy therefore requiring adoption of other strategies besides price and its related derivatives as a competitive strategy. Amongst the strategies is use merger and acquisitions to attain economies of scale.

Despite the liberalization of the market 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 (now operating as Vivo Kenya) 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, latest is Total Kenya that acquired all the assets of Chevron in Kenya (trading as Caltex) in June 2009. In September 2009, Raytec Metals Corporation merged with Lion Petroleum Inc in prospecting oil in two blocks in Manderu area of North Eastern Province Siddharth (2009). Other mergers were those of Kenya Oil Company Limited (Kenol) which merged with Kobil to form Kenol/Kobil Ltd in the year 2008. This study will focus on whether merger and acquisitions can provide a better platform of business instead of exiting from the Kenyan market.

1.2. Research Problem

The oil industry in Kenya has been involved with dynamic regulations that have affected directly to both operational and financial performance of the companies. The market has operated with price controls at some points regulated by ERC which has been challenging to the oil companies

to operate on. This has resulted with some of the companies exiting the market through the process of being acquired by other oil companies while some of the others have taken advantage of acquiring or merging with other companies for business continuity within the market. Kemal (2011) indicated that the motives behind mergers and acquisitions are economy of scale, economy of scope, increase market share and revenues, taxation, synergy, geographical and other diversification. This may be translated into better financial performance.

Owomoyela (2012) categorized the effects of M&A into long term and short term. In the long term effects, the expected synergistic characteristics of merger and acquisition can contribute to technological performance through the invention of new process-related technologies and new product related technologies by the combined companies. These new technologies (inventions) can eventually lead to improved profitability of companies if they are transformed into actual innovations, that is, new products and processes that are successfully introduced to the market. There can also be short-term effects of M & A when the acquiring company intends to only obtain access to Research and Development (R & D) and technological capabilities to simply produce an already existing, combined technological output that can result with increased profitability of the firm.

Ravenscraft and Scherer (1989) and Healy, Palepu and Ruback (1992) are two operating performance studies that have been particularly influential in reinforcing perceptions about the gains to acquiring firms. These two papers reach different conclusions about gains from mergers. However, each study has data limitations which raise concerns about the generality of the findings. Ravenscraft and Scherer found significant declines in the post merger profitability of the acquired portions of those firms in their investigation of more than 5000 mergers occurring between 1950 and 1975, while Healy, Palepu and Ruback found improvement in both sales and profits of the combined firms following the mergers.

The evidence on industry clustering of merger activity is important for interpreting the findings of operating performance studies. First, selecting an appropriate expected performance benchmark in the absence of a merger is crucial. Simply using the same firm's pre-merger performance will be unsatisfying if the merger transaction comes in response to an industry shock that changes the prospects for a meaningful fraction of the firms in the industry. An industry-based benchmark as employed by Healy, Palepu and Ruback (1992) will help absorb

this effect. Second, the tendency for merger activity to cluster through time by industry means that a short sample period will contain observations from only a few industries, making it difficult to generalize from these samples. Finally, if there is a common shock that induces merger activity at a particular point in time, there is no reason for it to be limited to just one industry or to affect all firms in an industry. Therefore, controlling for industry may not be sufficient to account for all cross-sectional correlation. A sample spanning a longer time period allows for statistical techniques that are better able to account for cross-sectional dependence.

Ndung'u (2011) conducted a research on effects of merger and acquisitions on financial performance of commercial banks in Kenya, on the sixteen banks that underwent merger and acquisition between 1999 and 2005. He concluded that there was improvement in financial performance after merger.

Wanguru (2011) carried out a study on the effect of mergers on profitability of firms in Kenya with attention to firms that had a merger between 2004 and 2008. Her observations were that, some of the merged companies' financial performance declined in the post merger period, others have displayed better profitability in the post merger and finally, Wanguru observed some others declined profitability declined immediately after the merger but gradually improved in the next two years.

Kilelo (2013) studied on mergers and acquisitions in the banking industry in Kenya. His main objective was to establish the determinants of M&A in the banking industry. He found that the banks venture into M&A in order to boost the capital base, market niche and returns to the investment and finally as an avenue to enter into the industry. His objective was to capture the reasons as to why the banking companies decide for an merger and acquisition decision that but not consider the performance of the merged banks thereafter.

Kioko (2013) studied on mergers and acquisition as an entry strategy by CFC Stanbic bank in the Kenyan market. The study focused on the ability of the bank having penetration into the Kenyan market. However, it is very important to consider if the M&A has potential of better financial performance in the market. The local studies done have not comprehensively outlined on the impact of M&A in the oil industry, this study will focus on the impact of M&A on the financial performance of oil companies in Kenya.

1.3. Objective of the Study

The key objective of the study is to establish the effect of merger and acquisition on the financial performance of oil companies in Kenya.

1.4. Value of the Study

The oil industry in Kenya has been very dynamic and challenging that has led exit of some oil companies and others having acquiring and merger processes. This study will be of importance to the executives and managers of OMCs that would be in considering on an acquisition or merger of their companies. It will render insight information of the expected results of merger and acquisition towards the financial performance of the new firm.

It will also be of importance to the government in making decisions of whether to facilitate or discourage mergers and acquisitions through its fiscal policy implementation.

The study will be of significant to the academicians and research personnel as it will provide insight information in this area.

The study would be used by the investors to know on how to act on information of merger and acquisition of any particular firm. Also the owners of the firm would have information on the impact of mergers and acquisition within the firm.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

(Kouser & Saba 2011), several studies discussed, tested and proposed empirical validations on M&A in last many decades. These researches have tested the economic impact of M&A through their pre and post-performance analysis, on industry, shareholders and company their selves. Moreover, they also proposed different methods for analyzing and attaining the success from mergers. And these proposals have positive impact on short-term and long-term both. This chapter summarizes the theories behind merger and acquisition together with information from other researchers who have carried out their research in the same field of study

2.2 Review of Theories

2.2.1 Free Cash Flow Theory

Jensen (1988), one major cause of takeover activity, the agency costs associated with conflicts between managers and shareholders over the payout of free cash flow, has received relatively little attention. Yet it has played an important role in acquisitions over the last decade. Managers are the agents of shareholders, and because both parties are self-interested, there are serious conflicts between them over the choice of the best corporate strategy. Agency costs are the total costs that arise in such cooperative arrangements. They consist of the costs of monitoring managerial behavior (such as the costs of producing audited financial statements and devising and implementing compensation plans that reward managers for actions that increase investors' wealth) and the inevitable costs that are incurred because the conflicts of interest can never be resolved perfectly. Sometimes these costs can be large, and when they are, takeovers can reduce them.

2.2.2 Resource Based Firm Theory

Beena (2011) acknowledges that the resource based firm theory is perhaps the most important theory that looks into why firms go for mergers or acquisitions. The theory states that firm's effectiveness is usually measured based on the superior performance by specific resources owned by the firm. Barney (1991) presented a concrete and comprehensive framework to identify the needed characteristics of firm resources in order to generate sustainable competitive advantage. These characteristics include whether resources are: valuable (in the sense that they exploit opportunities and/or neutralize threats in a firm's environment), rare among a firm's current and potential competitors, inimitable, and non-substitutable.

Barney defines these resources as the specific assets, firm attributes, organizational processes, capabilities, information, knowledge etc. These resources enable organizations to create strategies for superior performance and hence need to have four specific attributes- rarity, imperfect imitability, value and in substitutability. This resource is mostly the reason why firms go for acquisition or merger as it is very difficult to get these resources in parts and hence they go for whole acquisition. Extent of integration required can directly affect the time taken and cost savings for the integration activity. If the differences between the two firms were too large then time taken and cost will be high. If the extent of integration can be brought down by adapting processes and systems of one firm then it will be much easier, but sometimes the resistance from the other firm could be too high too. This extent of integration can be reduced by taking the best of both worlds in integration process.

2.2.3 Agency Theory

One important perspective of research on acquisitions and mergers is financial economics. Financial economics objective is to enhance wealth for the general economy and shareholders. The theoretical background of this is the agency theory. An agency relationship arises when one or more principals (e.g. an owner) engage another person as their agent (or steward) to perform a service on their behalf. Performance of this service results in the delegation of some decision-making authority to the agent. This delegation of responsibility by the principal and the resulting division of labor are helpful in promoting an efficient and productive economy. However, such

delegation also means that the principal needs to place trust in an agent to act in the principal's best interests.

A simple agency model suggests that, as a result of information asymmetries and self interest, principals lack reasons to trust their agents and will seek to resolve these concerns by putting in place mechanisms to align the interests of agents with principals and to reduce the scope for information asymmetries and opportunistic behavior. Agents are likely to have different motives to principals. They may be influenced by factors such as financial rewards, labor market opportunities, and relationships with other parties that are not directly relevant to principals. This can, for example, result in a tendency for agents to be more optimistic about the economic performance of an entity or their performance under a contract than the reality would suggest. Agents may also be more risk averse than principals. As a result of these differing interests, agents may have an incentive to bias information flows. Principals may also express concerns about information asymmetries where agents are in possession of information to which principals do not have access.

Tsuji (2011), agency costs and the agency theory are important issues both in corporate governance and capital structure. The separation of ownership and control in a corporation, which is a source of agency conflicts, may lead to managers' insufficient work effort. More concretely, these agency conflicts result in choosing inputs or outputs that suit managers' own preferences, and a corporation fails to maximize its value. 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 Transaction Cost Theory

Transaction costs applies to vertical merger and acquisition aimed at reducing uncertainty or the cost of procuring a particular factors of production. Following the transaction cost theory Coase (1937), firms evaluate the relative costs of alternative governance structures (spot market transactions, short term contracts, long-term contracts, vertical integration) for managing transactions. Transaction costs could be defined as the costs of acquiring and handling the information about the quality of inputs, the relevant prices, the supplier's reputation, and so on. Contractual agreements are costly: costs have to be borne in order to negotiate and write the terms of the arrangements, to monitor the performance of the contracting party, to enforce the contracts. Firms merge as a way of economising on transaction costs in a world of uncertainty, where contractual arrangements are too expensive.

2.2.5 Modigliani – Miller Theorem

According to Modigliani – Miller Theorem, with perfect capital markets, value can neither be created nor destroyed by repackaging a firm's securities as long as the repackaging leaves the total cash flows of the firms unchanged. Similarly, any merger or acquisition that has no effect on the after cash flow of the firm will not create or destroy value. This means that in order for a merger or acquisition to create value, the after cash flows of the combined firm must exceed the sum of the after tax cash flows of the individual firms before the merger.

2.2.6 Corporate Control Theory

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.

2.2.7 Financial Synergies Theory

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.

2.2.8 Managerial Hubris Theory

According to the managerial hubris theory, 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) as a result of overconfidence by the managers. 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.

2.2.9 Industry Shock Theory

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 Determinants of Financial Performance in Oil Companies

Financial performance is the process of measuring the results of a firm's policies and operations in monetary terms. It is used to measure firm's overall financial health over a given period of time and can also be used to compare similar firms across the same industry or to compare industries or sectors in aggregation. Different measures have been used to determine financial performance of a firm which includes return on sales reveals how much a company earns in relation to its sales, return on assets determines an organization's ability to make use of its assets and return on equity reveals what return investors take for their investments.

The empirical literature examines how financial factors, such as profitability, liquidity, efficiency have an influence on the firms' financial performance and growth. Debt leverage is measured by the ratio of total debt to equity (debt/equity ratio). It shows the degree to which a business is utilizing borrowed money. Companies that are highly leveraged may be at risk of bankruptcy if they are unable to make payments on their debt; they may also be unable to find new lenders in the future. Leverage is not always bad, however; it can increase the shareholders' return on their investment and make good use of the tax advantages associated with borrowing Khamrui, (2012).

Liquidity refers to the degree to which debt obligations coming due in the next 12 months can be paid from cash or assets that will be turned into cash. It is usually measured by the current assets to current liabilities (current ratio). It shows the ability to convert an asset to cash quickly and reflects the ability of the firm to manage working capital when kept at normal levels. A firm can use liquid assets to finance its activities and investments when external finance is not available or it is too costly. On the other hand, higher liquidity would allow a firm to deal with unexpected contingencies and to cope with its obligations during periods of low earnings.

The size of the firm affects its financial performance in many ways. Large firms can exploit economies of scale and scope and thus being more efficient compared to small firms. In addition, small firms may have less power than large firms; hence they may find it difficult to compete with the large firms particularly in highly competitive markets. On the other hand, as firms become larger, they might suffer from inefficiencies, leading to inferior financial performance Khamrui, (2012).

This is especially the resources available to the company to explain its success. These resources are both tangible and intangible entities that enable a company to make an offer value for some market segments (Hunt, 2000). In this approach, the differences between the companies are linked to sources of efficiency and effectiveness introduce all possible distinctions between companies: distinction in terms of market share, in the configuration activities and, at the level of managerial skills. These elements distinguish competitive positions give different companies in a given area. According to Hunt (2000), the most successful companies are those that benefit from better skills and better resources, allowing them later to create offers effective, efficient and value for customers.

2.4 Review of Empirical Studies

Various empirical studies on corporate mergers and acquisitions have been done with focus to the effect of merger and acquisition on firm performance. This is because Mergers & Acquisitions have been the commonest method of corporate strategy to improve firm performance.

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.

Ravenscraft & Scherer (1989) examine target firm profitability over the period 1975 to 1977 using Line of Business data collected by the Federal Trade Commission. The FTC collected data for 471 firms from 1950 to 1976 by the business segments in which the firms operated. Ravenscraft & Scherer compared the post merger performance of the acquired firms with the performance of non acquired control group firms in the same industry and found that the target lines of business suffer a loss in profitability following the merger. They concluded that mergers destroy value on average, which directly contradicts the conclusion drawn from the announcement-period stock market reaction.

Healy, Palepu & Ruback (1992) examined post-merger operating performance for the 50 largest mergers between 1979 and 1984. In particular, they analyzed the operating performance for the combined firm relative to the industry median. They found that merged firms experience improvements in asset productivity, leading to higher operating cash flows relative to their industry peers. Interestingly, their results show that the operating cash flows of merged firms actually drop from their pre-merger level on average, but that the non-merging firms in the same industry drop considerably more. Thus, the post-merger operating performance improves relative to the industry benchmark.

Franks, Harris, & 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.

Rhoades (1993) studied the impact of mergers in banking industry on efficiency and profitability considering both the domestic and cross border mergers. It discussed the cost and profit efficiency analysis of 33 bank-to-bank mergers which shows that the most of the domestic mergers improves the cost efficiency and little improvement of profit efficiency whereas little improvement in the profit efficiency and no improvement in the cost of efficiency in the cross border mergers.

Andre, Kooli & 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 & L'Her also found that cross border deals perform poorly in the long run.

Sufian (2004) focused on the efficiency effects of M&A of banks in Malaysia. For this purpose Malaysian commercial banks were taken to analyze the technical efficiencies during the merger year, and study pre and post-merger period. Their results proved an overall increase in efficiency in the sample period which is around 95.9%. They also concludes that merger program was successful and the small size Malaysian banks. Although the financial sector especially banks took advantage and got benefits from mergers but some of the large banks faced certain inefficiencies of large scale from this. Sufian & Habibullah (2010) observes Malysian banking sector on the basis of their technical efficiency after merger and acquisition. Study found a higher mean technical efficiency level when they compare it with the pre-merger period.

Mantravadi & Reddy (2008) studied pre and post-merger performance in India and target the acquiring firms from diverse sectors and different industries but their major emphasis was on measurement of operating performance of the firms through financial ratios. They select the sample of all the mergers between public limited ad trading firms during 1991-2003. The findings of this study did not show much impact in the post-merger operating performance of the firms in different industries in India.

Badreldin & Kalhoefer, (2009) research is based on Egyptian banks which have faced Merger or acquisition during the era of 2002-2007. They calculated companies Return on Equity (RoE) in order to the level of progress and success of banking reforms in strengthening and consolidating this sector. Their analysis suggested an increase in the performance when companies are compared with the pre-merger performance. It is concluded in the study that M&A in the Egyptian banking sector's profitability showed a significant improvement and a small positive impact on the credit risk position. But these observations are not similar to the current process.

Agrawal, Jaffe & Mandelker (1992) examined the post-merger performance of acquiring firms. They found 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 & 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.

Kilelo (2013) studied on mergers and acquisitions in the banking industry in Kenya. His main objective was to establish the determinants of M&A in the banking industry. He found that the banks venture into M&A in order to boost the capital base, market niche and returns to the investment and finally as an avenue to enter into the industry. His objective was to capture the reasons as to why the banking companies decide for an merger and acquisition decision that but not consider the performance of the merged banks thereafter.

Kioko (2013) studied on mergers and acquisition as an entry strategy by CFC Stanbic bank in the Kenyan market. The study focused on the ability of the bank having penetration into the Kenyan market. However, it is very important to consider if the has the potential of better financial performance in the market.

2.5 Summary of Literature Review

Different techniques of measuring the effect of M&As have been used by different authors in the above studies. The effects were measured through measuring the shareholders value, operating cash flow, profitability of the firm. The authors have found varying results on the effect of M&A on a firm's performance some having positive effects to the firms and others having negative effects.

Several theories have arisen as to the reason why M&As take place in the firms. 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). 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 & Majluf, 1984).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This session shows the procedure followed to complete the study. It involves details on the data collection, measurement and data. It 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.

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 financial performance of oil companies in Kenya. Causal research design is consistent with the study's objective which is to determine the effect of mergers and acquisition on liquidity, leverage, long-run profitability and efficiency of oil companies in Kenya.

3.3 Population

Target population in statistics is the specific population about which information is desired. According to Mugenda & 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. In this study, the target population was the oil companies in Kenya that have merged between 2003 and 2013. Appendix 1 shows the list of Oil Companies in Kenya.

3.4 Sample Design

The sample selected in this study comprises of all the oil the companies that have undergone merger and acquisition process in Kenya in the period 2003 to 2013. The companies that have

undergone merger and acquisition during this period are KenolKobil Limited, 2008, Vivo Kenya limited (when trading as Shell) –BP in 2006 and Total Kenya Ltd acquiring Chevron Company Ltd (trading as Caltex in Kenya) in 2009.

3.5 Data Collection

The study has used secondary data gathered from financial statements of the various companies involved in merger and acquisition process ranging from three year before the M&A to three years after the M&A process so as to help the researcher achieve the research objective stated.

3.6 Data Analysis

The secondary data collected was processed, analyzed, interpreted and presented in such a manner that it was clear, precise and unambiguous. This data was quantified and coded using descriptive statistics. The Statistical package for social sciences (SPSS version 16) was used to describe the collected data, sort and sift through and analyze it. Measures of central tendency, the mean in particular, were used in data analysis together with tests of significance.

3.6.1 Analytical Model

Comparable data analysis was used to measure the effect of acquisition and merger on the financial performance of Oil Companies in Kenya. The study used current ratio, debt equity ratio, net income ratio and receivables turnover representing liquidity, leverage, long-run profitability and efficiency respectively to determine the financial performance of the oil company in both the pre merger and post merger periods. The measurement of financial performance was estimated by Return of Equity (ROE)

Regression model was used to analyze the data presented. The regression model used was in the form;

$$Y_i = \beta_0 + \beta_1 X_{i,1} + \beta_2 X_{i,2} + \beta_3 X_{i,3} + \beta_4 X_{i,4} + \epsilon$$

Where; $i= 1, 2, 3, 4, \dots, k$ are the number of observations from the sample;

β_0 = constant free term of the equation

$\beta_1, \beta_2, \beta_3, \beta_4$ = coefficient of independent variable

X_1 = Current Ratio

X_2 = Debt to Equity Ratio

X_3 = Net Income Margin

X_4 = Receivable Turnover

ϵ = error term of equation

Y_i = Financial Performance estimated by Return on Equity (ROE).

3.6.2 Test of Significance

The study established the association between pre-and post-merger or acquisition performance by use of T-Test Statistic. T statistic is used to compare the actual sample mean with the hypothesized population mean. The hypothesized population mean was presented by the pre-merger data in the study. In this case, the hypothesis set for the study was;

H_0 : Merger and acquisitions is associated with increase in financial performance

The hypothesis was tested at 0.05 level of significance.

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATIONS OF FINDINGS

4.1 Introduction

This chapter entails the data presentation, analysis and interpretation of the findings of the project. The statistical package for social sciences software was used to perform the analysis. Descriptive and regression analysis has been utilized to analyze the findings in this study. Data was collected from audited financial reported for the selected companies.

4.2 Data Presentation

4.2.1 Descriptive Data Presentation

The following table gives the ratios of the collected variables on the pre-merger period. The total of observations sums to $n = 12$.

Table 4.2.1 Pre–Merger/Acquisition Ratio Results

Period	ROE	Current Ratio	Debt to Equity Ratio	Net Income Margin	Receivable Turnover
1	0.1652	1.3058	1.6718	0.0200	11.9360
2	0.1674	1.5154	1.2868	0.0206	13.9089
3	0.1650	1.4817	1.2581	0.0201	13.5990
4	0.1661	1.3133	1.6814	0.0201	12.0046
5	0.1463	3.2265	1.1528	0.0177	12.0299
6	0.1451	3.2003	1.1434	0.0176	11.9324
7	0.1439	3.1742	1.1341	0.0174	11.8348
8	0.1454	3.0287	1.0821	0.0166	11.2924
9	0.1229	3.6851	1.5763	0.0174	14.7639
	0.1307	5.7276	2.4500	0.0271	22.9465

10					
11	0.1408	4.2205	1.8054	0.0199	16.9089
12	0.1297	2.8875	1.2351	0.0136	11.5681
Mean	0.1474	2.8972	1.4564	0.0190	13.7271

Source: Research Findings

The following table gives the descriptive statistics of the collected variables on the pre-merger period

Table 4.2.2 Pre–Merger/Acquisition Descriptive Statistics

	PRE MERGER		
	Mean	Std. Deviation	N
ROE	0.1474	0.01548	12
Current Ratio	2.8972	1.33593	12
Debt to Equity Ratio	1.4564	0.40132	12
Net Income Margin	0.0190	0.00325	12
Receivable Turnover	13.7271	3.33973	12

Source: Research Findings

The following table gives the ratios of the collected variables on the post-merger period. The total of observations sums to n = 12.

Table 4.2.3 Post–Merger/Acquisition Ratio Results

Period	ROE	Current Ratio	Debt to Equity Ratio	Net Income Margin	Receivable Turnover
1	0.0776	0.5002	0.8409	0.0054	5.8332
2	0.0882	0.5685	0.9557	0.0061	6.6299
3	0.0973	0.6276	1.0550	0.0068	7.3185
4	0.0967	1.2065	2.0281	0.0130	14.0693
5	0.0470	1.2467	1.9249	0.0112	4.7279
	0.4055	1.1947	1.9621	0.0087	17.9665

6					
7	0.0363	1.2375	1.9512	0.0067	9.8486
8	0.0954	1.2366	1.9512	0.0128	10.1719
9	0.2007	1.2302	1.7350	0.1306	2.4896
10	0.0810	1.2578	2.1804	0.0245	4.1037
11	0.0707	1.2685	2.0307	0.0125	6.5794
12	0.0660	1.2404	2.1818	0.0083	9.9059
Mean	0.1135	1.0679	1.7331	0.0206	8.3037

Source: Research Findings

The following table gives the descriptive statistics of the collected variables on the post-merger period

Table 4.2.4 Post–Merger/Acquisition Descriptive Statistics

	POST MERGER		
	Mean	Std. Deviation	N
ROE	0.1135	0.10054	12
Current Ratio	1.0679	0.30487	12
Debt to Equity Ratio	1.7331	0.48818	12
Net Income Margin	0.0206	0.03504	12
Receivable Turnover	8.3037	4.39147	12

Source: Research Findings

4.2.2 Regression Analysis

To establish the relationship between M&A and financial performance of oil companies in Kenya, a multiple regression analysis was conducted. The regression model used was as follows;

$$ROE = \beta_0 + \beta_1(\text{Current Ratio}) + \beta_2(\text{Debt to Equity Ratio}) + \beta_3(\text{Net Income Margin}) + \beta_4(\text{Receivable turnover}) + \varepsilon$$

Through regression analysis the results of correlation, coefficient of determination and analysis of variance (ANOVA) were also attained. Correlation sought to show the nature of relationship between dependent and independent variables while coefficient of determination showed the strength of the relationship. ANOVA was conducted at 95% confidence level.

Table 4.2.5 Model of Goodness of Fit

Model Summary^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	0.744 ^a	0.553	0.459	0.05328	2.038

a. Predictors: (Constant), Receivable Turnover, Debt to Equity Ratio, Net Income Margin, Current Ratio

b. Dependent Variable: ROE

Source: Research Findings

Regression analysis was used to establish the relationship between ROE and the factors that affect the variables. The results showed a correlation value of 0.744 which depicts that there is a good linear dependence of ROE on current ratio, debt to equity ratio, net income and receivable turnover.

The adjusted R^2 is known as coefficient of determination and it shows the variation in effect of merger and acquisition and financial performance. The study findings indicate that the goodness of fit model was adequate. This was reported by r squared of 0.553 which means that 55.3% of the variation in ROE (financial performance) is explained by changes in current ratio (liquidity), debt to equity ratio (solvency), net income ratio (profitability) and receivable turnover (efficiency). The correlation coefficient of 74.4% means that the dependent variables have a strong correlation with the independent variable.

Table 4.2.6 Correlation Analysis

		Return on Equity	Current Ratio	Debt to Equity Ratio	Net Income Margin	Receivable Turnover
Pearson Correlation	Return on Equity	1.000				
	Current Ratio	0.100	1.000			
	Debt to Equity Ratio	-.036	0.100	1.000		
	Net Income Margin	0.242	0.035	0.120	1.000	
	Receivable Turnover	0.443	0.673	0.204	-0.265	1.000
Sig. (1-tailed)	Return on Equity	.				
	Current Ratio	.321	.			
	Debt to Equity Ratio	0.434	0.320	.		
	Net Income Margin	0.127	0.435	0.288	.	
	Receivable Turnover	0.015	0.000	0.170	0.105	.
N	All variables	24	24	24	24	24

Source: Research Findings

According to the analysis, liquidity, profitability and efficiency ratios are positively correlated to the financial performance of the company while solvency ratio is negatively correlated.

Table 4.2.7 Analysis of Variance**ANOVA^b**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	0.067	4	0.017	5.881	0.003 ^a
	Residual	0.054	19	0.003		
	Total	0.121	23			

a. Predictors: (Constant), Receivable Turnover, Debt to Equity Ratio, Net Income Margin, Current Ratio

b. Dependent Variable: ROE

Source : Research Findings

ANOVA was conducted to determine the differences in the means of the dependent and independent variable thus show whether a relationship exist between the two. The p-value of 0.003 means that ROE has a significant joint relationship with current ratio, debt to equity ratio, net income and receivable turnover at 5% level of significance.

Table 4.2.8 Regression coefficient results

		Coefficients^a				
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.049	0.045		1.071	0.297
	Current Ratio	-0.033	0.012	-0.602	-2.753	0.013
	Debt to Equity Ratio	-0.041	0.025	-0.258	-1.612	0.124
	Net Income Margin	1.704	0.507	0.573	3.361	0.003
	Receivable Turnover	0.016	0.004	1.052	4.522	0.000

a. Dependent Variable: ROE

Source: Research Findings

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

$$Y = 0.049 - 0.033 X_1 - 0.041X_2 + 1.704 X_3 + 0.016 X_4$$

4.3 Summary and Interpretation of Findings

This section summarizes the results of the study. The study findings indicate that Return on Equity (ROE) mean decreased from 0.1474 to 0.1135 after Merging/Acquisition. This implies that either returns of the merged/acquired companies have decreased or the shareholder equity of the firm has increased after the merger/acquisition process. The study findings have observed that the merger/acquisition processes that have taken place in the oil industry in Kenya have affected the capital structure of the new companies by having additional shareholding. This has led to increase in share equity of the merged/acquired firm thus reducing the return on equity. Reduction in returns could have been attributed by finance cost incurred on the loan taken by

Total Kenya Limited to facilitate acquisition of Chevron Kenya Limited and also loss made by KenolKobil Limited as a result of the forward contract on foreign currency that both occurred on the post-merger period.

The study findings indicate that the liquidity mean of the merged/acquired company decreased from 2.8972 to 1.0679. The decrease is a result of lower current assets or higher current liabilities during post-merger/acquired period compared to the pre-merger/acquisition period. The decline could be as a result of more commitments by the merged/acquired firm.

From the study findings, indicate that the post merger/acquisition is more insolvent than the pre merger firm. The debt equity average increased from 1.4564 to 1.7331 implying that the firms were more indebted than the pre-merger/acquisition process.

The profitability mean of the firms improved from a net a margin of 0.0190 to 0.0206. Observations made on the study by Wanguru (2011) study on the effect of mergers on profitability of firms in Kenya with attention to firms that had a merger between 2004 and 2008 was that some of the merged companies' financial performance declined in the post merger period while others displayed better financial performance. With regard to this study, the profitability of the M&As in the oil industry in Kenya increases on the post merger period.

The efficiency average of the merged/acquired firm is seen to have declined in comparison of the pre-merger period. The rate decreased from 13.7271 to 8.3037. The decrease could have been influenced by either decrease in sales or increase of the accounts receivable. The results of this study, have established that the decrease of receivable turnover has been mainly influenced by increase in the accounts receivable at a higher rate than that of sales for the merged/acquired firm. Increase of the accounts turnover could have been attributed to non settlement of the accounts on time.

Regression results indicate that the goodness of fit for the regression model between independence and dependent variables are satisfactory having attained a correlation value of 0.744. An R^2 of 0.553 indicates that 55.3% of the variances on ROE are explained by the variances in the independent variables. This also implies that 44.7% of the variances in financial performance cannot be explained by the independent variables and is actually attributed to variables not included in the model.

ANOVA statistics indicate that the overall model was significant. The p-value of 0.003 means that ROE has a significant joint relationship with current ratio, debt to equity ratio, net income and receivable turnover at 5% level of significance.

The regression above shows that when all other variables have a value of zero, the financial performance of the M&A oil company in Kenya is 0.049. Unit increase of liquidity and solvency decrease the financial performance by 0.033 and 0.041 respectively while unit increase of profitability and efficiency increases the financial performance by 1.704 and 0.016 respectively. The critical values attained are within the acceptance region of the study hypothesis thus M&A is associated with increase in financial performance.

Ndung'u (2011) concluded that there was improvement in financial performance after merger of M&As in the commercial banks of Kenya between 1999 and 2005. While Owomoyela (2012) categorized the effects of M&A into long term and short term and indicated that the expected synergistic characteristics of merger and acquisition can contribute to technological performance through the invention of new process-related technologies and new product related technologies by the combined companies. These new technologies (inventions) can eventually lead to improved profitability of companies. With regard to this study, the oil industry in Kenya shows a decrease in financial performance after M&A process.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The study was carried out with an objective of establishing the effect of merger and acquisition on the financial performance of oil companies in Kenya. The research design adopted was causal research design. The study focused on the mergers and acquisitions that have occurred between year 2003 and 2013 within the industry. The population of this study was all the oil companies' registered to operate their commercial activities in Kenya. The study sample comprised of two oil companies listed in the Nairobi Stock Exchange market namely KenolKobil Limited and Total Kenya Limited.

Secondary data from the audited financial statements of the companies was used in this study. Analysis of the data acquired was performed through use of the SPSS software (version 16). Both descriptive and regression analysis methods were used to establish the effect of merger and acquisition on the performance of oil industries in Kenya.

Regression analysis was conducted to establish the relationship between financial performance and the independent variables that is the liquidity, solvency, debt to equity ratio, profitability and efficiency of the oil companies in Kenya.

The study findings indicate that the goodness of fit model was adequate. This was reported by r squared of 0.553 which means that 55.3% of the variation in ROE (financial performance) is explained by changes in current ratio (liquidity), debt to equity ratio (solvency), net income ratio (profitability) and receivable turnover (efficiency). The correlation coefficient of 74.4% means that the dependent variables have a strong correlation the independent variable.

Analysis of the ANOVA results showed that there is a significant joint relationship between financial performance and liquidity, solvency, profitability and efficiency of p -value 0.003 at 5% level of significance.

5.2 Conclusion

Corporate mergers and acquisitions are aimed at amplifying efficiency, enhancing competitive advantage, achieving synergy and improving firm value. Mergers and Acquisitions pursue the profitability, liquidity and solvency objectives of an organization. The study was carried out to determine whether improvements occur after the merger and acquisition are undertaken. The analysis and results show that oil companies performed lesser in the post- merger/acquisition era as compared to the pre-merger/acquisition era. This is supported by the fact that merging/acquisition had a significant impact on the ROE, which is the overall standard measure of financial performance due to the statistical significance it has on ROE as well as total asset ratio.

The firms are motivated for mergers or acquisitions for various reasons with realization that business combinations provide an opportunity to create new economic value for their shareholders. This new value can be created through taking advantage of the economies of scale to be achieved through the combination as a result of the new firm performing a function more effectively more than the two separate firms. The value would also be increased by combining firms with complimentary resources for efficiency and effectiveness in the business operations. Other potential areas of increasing value to shareholder would be in capturing of tax benefits on the merger and acquisition procedure, increasing product markets rates as a result of the small firms turning to be dominant firm in the industry and finally adding value by improving the target company's management. Through this, the new firms are expected to increase efficiency, profitability, liquidity and solvency in their operations.

According to the study, the efficiency of the merged/acquired firm decreased. This was mainly attributed to increased volume of sales but less effort in collection of the credit sale amount and also the credit sales of the previous company took longer period of collection resulting to low the efficiency of the new firm in terms of the turnover.

Liquidity and solvency of the firms, seems to have deteriorated in the merged/acquired entities. This resulted due to increased debt to enhance owning of the target companies. The merged/acquired firms also experienced more commitments in financing costs that eventually reduced the liquidity of the firms.

The study established that the profitability measured by the net income margin improved of the merged/acquired firm. This is a result of the synergies that have been created leading the companies to enjoy economies of scale in their operations.

5.3 Recommendations to Policy and Practice

The study recommends that the companies with plans on mergers/acquisitions should prepare on terms of the labor forces required to retain the customers after the merger/acquisition process. This can be achieved by retaining all the employees of the acquired/merged company if possible. The alternative method is by having recruitment of new staff in the company to increase the effort of the existing staff.

The study further recommends that the merging/acquiring firm to internally generate income to facilitate the merging/acquiring and have less borrowing. This is to enable the firm to have better liquidity and solvency.

The study established that the profitability measured by the net income margin improved of the merged/acquired firm. This is a result of the synergies that have been created leading the companies to enjoy economies of scale in their operations.

The study recommends that the management should instill discipline upon itself by ensuring good corporate governance, promote technological progress and increase its paid up capital regardless of the statutory requirements so that the continued existence of the firm is not jeopardized after undergoing mergers and acquisition. Management should not only undertake mergers and acquisitions in order to improve operation and sustain failing businesses but also improve their competitiveness and financial standing. Management should come up with a sound strategy towards asset and liability management so as to avert the problem of mismatching investments and also the quality of assets should be enhanced. Management should put into consideration the degree of transferability and marketability of assets invested in so that these assets can provide liquidity to the firm with ease.

5.4 Limitations of the Study

The short period of time that has been available to carry out this research has been a key a challenge. A longer period of time of carrying out the study would facilitate collecting of data in a comprehensive manner and evaluation of other effects of financial performance of oil companies in Kenya.

Some companies particularly the private owned companies do not publicly avail their financial statements due to their operation nature. This made the data collection a bit hectic as well as time consuming. The study reconsidered to use the data of the data available on the public phenomena. The data used in this case is from the listed oil companies in the Nairobi Stock Exchange namely KenolKobil Limited and Total Kenya Limited.

The period of study considered is short that is three years pre and post merger. A longer period of time can be considered in future studies. The companies studied had a merger or acquisition at close year 2008 and 2009 which would have been affected with other microeconomic and macroeconomic factors effects leading to different results from the actual results.

A small sample of the companies that have merged/acquired has been selected due to the fact that not many oil companies that undergone mergers and acquisition during the study period. The results may not be very conclusive.

5.5 Areas for Further Research

More research to be done using a base rate company or using the industry results for comparison purposes. This will help to detect any other factor affecting the financial performance of the oil companies in Kenya. The researcher to exclude the additional factors to establish the actual effect of M&A on financial performance of the oil companies in Kenya.

Further research in other sectors that have engaged in mergers and acquisitions should be embarked on so as to obtain further insights. This is because the type of industry may make a difference to the pre-merger/acquisition and post-merger/acquisition financial performance of firms. Extensive research has been already been carried out on effect of mergers and acquisition on the financial performance of the banking sectors and thus it is important to look into other sectors such as; insurance companies, manufacturing companies, IT and communications firms to enable to determine whether mergers and acquisitions do have a significant impact on the

financial performance of firms. In addition, it is important to study the effect of mergers and acquisitions on shareholder value of the stated firms and also oil companies.

Further research to be done involving companies not listed in the NSE to establish the effect of financial performance from the merger and acquisition processes. This will have a comprehensive view of entire industry in Kenya.

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APPENDICES

APPENDIX 1: List of Oil Companies in Kenya as at 31.03.2014

No	Company Name
1	AFRIOIL INTERNATIONAL LIMITED
2	AINUSHAMSI ENERGY LTD
3	ALAMANA INVESTMENTS LTD
4	ALBA PETROLEUM LTD
5	AMANA PETROLEUM(KENYA) LTD
6	ASTROL PETROLEUM CO.LTD
7	AXON ENERGY LIMITED
8	BAKRI INTERNATIONAL ENERGY(K)
9	BANODA OIL LTD
10	CAPE SUPPLIERS LTD
11	CENTER STAR COMPANY LTD
12	CITY OIL (K) LTD
13	DALBIT PETROLEUM LTD
14	EAST AFRICAN GASOIL LTD
15	ECO OIL KENYA LTD
16	ELIORA ENERGY LIMITED
17	EMKAY INTERNATIONAL LTD
18	ENGEN PETROLEUM LTD
19	ESSAR PETROLEUM (EA) LTD
20	FAST ENERGY LTD
21	FINEJET LTD
22	FOSSIL FUELS LTD
23	FUTURES ENERGY CO. LTD
24	GALANA OIL KENYA LTD
25	GAPCO KENYA LTD
26	GLOBAL PETROLEUM PRODUCTS KENYA
27	GULF ENERGY LTD
28	HASHI ENERGY LTD
29	HASS PETROLEUM KENYA LTD
30	ILADE OIL COMPANY LIMITED
31	INTOIL LTD
32	JADE PETROLEUM LTD
33	JAGUAR PETROLEUM LTD
34	KAMKIS TRADING COMPANY LTD
35	KENCOR PETROLEUM LTD
36	KENOLKOBIL LTD

No	Company Name
40	LUQMAN PETROLEUM LIMITED
41	MOGAS KENYA LTD
42	MOIL KENYA LIMITED
43	MULOIL LIMITED
44	NAFTON OIL COMPANY
45	NATIONAL OIL CORPORATION OF KENYA
46	OCEAN ENERGY LIMITED
47	OIL CITY LTD
48	OILCOM KENYA LTD
49	OILPOINT KENYA LTD
50	OLYMPIC PETROLEUM LTD
51	ONE PETROLEUM LTD
52	ORIX OIL (KENYA) LTD
53	ORYX ENERGIES KENYA LTD
54	PETRO OIL KENYA LTD
55	PETROSUN K LIMITED
56	PREMIUM PETROLEUM CO. LTD
57	PRIME GAS INVESTMENT LTD
58	PRIME REGIONAL SUPPLIES
59	RAMJI HARIBHAI DEVANI LTD
60	RANWAY TRADERS LTD
61	REGNOL OIL (K) LTD
62	RIVA PETROLEUM DEALERS LTD
63	ROYAL ENERGY (K) LTD
64	SAFARI PETROLEUM LTD
65	SOCIETE PETROLIERE KENYA LTDO
66	SOVEREIGN OIL LIMITED
67	STABEX INTERNATIONAL LTD
68	TIBA OIL COMPANY LTD
69	TOPAZ PETROLEUM LTD
70	TOSHA PETROLEUM (K) LTD
71	TOTAL KENYA LIMITED
72	TOWBA PETROLEUM CO. LTD
73	TRADIVERSE KENYA LIMITED
74	TRISTAR TRANSPORT LIMITED
75	TROJAN INTERNATIONAL LTD

37	KEROKA PETROLEUM LTD
38	KOSMOIL PETROLEUM(EA) LTD
39	LIBYA OIL KENYA LTD

76	ULTRA PETROLEUM LTD
77	UNITED ENERGY LIMITED
78	VIVO ENERGY KENYA LTD

Source: Petroleum Institute of East Africa (PIEA)

APPENDIX 2: Pre - Merger/Acquisition Ratio Results

Period	ROE	Current Ratio	Debt to Equity Ratio	Net Income Margin	Receivable Turnover
1	0.1652	1.3058	1.6718	0.0200	11.9360
2	0.1674	1.5154	1.2868	0.0206	13.9089
3	0.1650	1.4817	1.2581	0.0201	13.5990
4	0.1661	1.3133	1.6814	0.0201	12.0046
5	0.1463	3.2265	1.1528	0.0177	12.0299
6	0.1451	3.2003	1.1434	0.0176	11.9324
7	0.1439	3.1742	1.1341	0.0174	11.8348
8	0.1454	3.0287	1.0821	0.0166	11.2924
9	0.1229	3.6851	1.5763	0.0174	14.7639
10	0.1307	5.7276	2.4500	0.0271	22.9465
11	0.1408	4.2205	1.8054	0.0199	16.9089
12	0.1297	2.8875	1.2351	0.0136	11.5681
Mean	0.1474	2.8972	1.4564	0.0190	13.7271

Source : Research Findings

APPENDIX 3: Post - Merger/Acquisition Ratio Results

Period	ROE	Current Ratio	Debt to Equity Ratio	Net Income Margin	Receivable Turnover
1	0.0776	0.5002	0.8409	0.0054	5.8332
2	0.0882	0.5685	0.9557	0.0061	6.6299
3	0.0973	0.6276	1.0550	0.0068	7.3185
4	0.0967	1.2065	2.0281	0.0130	14.0693
5	0.0470	1.2467	1.9249	0.0112	4.7279
6	0.4055	1.1947	1.9621	0.0087	17.9665
7	0.0363	1.2375	1.9512	0.0067	9.8486
8	0.0954	1.2366	1.9512	0.0128	10.1719
9	0.2007	1.2302	1.7350	0.1306	2.4896
10	0.0810	1.2578	2.1804	0.0245	4.1037
11	0.0707	1.2685	2.0307	0.0125	6.5794
12	0.0660	1.2404	2.1818	0.0083	9.9059
Mean	0.1135	1.0679	1.7331	0.0206	8.3037

Source : Research Findings