THE IMPACT OF ACQUISITIONS ON FINANCIAL PERFORMANCE OF FIRMS IN THE TELECOMMUNICATION INDUSTRY IN KENYA

BY

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DECLARATION

This research project is my original work and has not been presented for examination or 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

I dedicate this research project in all sincerity to my family for their continuous support and encouragement during my study.

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LIST OF ABBREVIATIONS

CA	:	Total Current assets
CL	:	Current liability
CMA	:	Capital Market Authority
D/E	:	Debt over Equity
D/E	:	Total debt to total equity
GDP	:	Gross Domestic Product
LTD	:	Limited
NSE	:	Nairobi Securities Exchange
ROA	:	Return on Assets
ROE	:	Return on Equity
Sig	:	Significance
SMEs	:	Small and Medium Enterprises
SPSS	:	Statistical Package for Social Science

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ABSTRACT

There is Increasing competition arising from the changing global market which has resulted in firms finding it difficult to remain competitive. Acquisitions seem to be a very popular thing to the corporates in the current world. Empirically, studies have found conflicting results of financial performance before and after acquisitions. In view of these contradictory results, the question of the determinants of finance decisions in these acquisitions remains pertinent. This study aimed to close this gap and give a clear picture on the impact of takeovers on the performance of the firms that acquire other firms. This research adopted a descriptive research design in order to determine the impacts of YU mobile acquisition on Safaricom Ltd and Airtel financial performance. The target population under study consisted of Safaricom Ltd and Airtel Companies in Kenya. The target population for this study comprised of finance departments of Safaricom and Airtel Kenya. Regression model was used to determine the relationship between the variables. Data was analyzed by Statistical Package for Social Science (SPSS Version 20.0) program. Quick ratio, Current ratio, Total asset ratio and Debt/Equity ratio have a significant relationship with the Return on Assets. The study also concludes that acquisition of firms can also lead to an increase in liability of the firm that might exceed the net worth of the acquiring firm and hence leads to a positive increase of Total debt ratio that might affect the financial performance of the acquiring firm. The study finally recommends that during acquisition the acquiring firm should ensure that the total liabilities should not exceed the net worth of the business by a bigger margin to mitigate on financial performance of an acquiring firm.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

In the recent past, there is increased competition arising in the global market which is pushing many organizations to adjust and do everything possible to be competitive. It is evident that unlike before firms are ensuring that their current resources and skills as well as strategies are aligned to ensure they survive to not only currently but into the future. The management need come up with innovative ways to ensure that the firms they manage are competitive and engage into partnerships that will lead to great benefits. There are modified threats as well as opportunities due the advanced competitive environment we operate in. These emerging conditions have forced many firms to change the way they operate to survive. Due to this, many firms are opting to merge so that they both have a better competitive advantage (Gupta, 2012). Mergers and acquisitions have become one of the most common option the firms a taking to obtain the resources and skills to enhance their earnings.

Piaskoki and Finkelstein (2004), indicated that in order for firms to be more efficient in their operation acquisitions are inevitable. This will increase economies of scale of this firms. There are also other areas where this firms become efficient such as increased economies of scope in production and consumption. There is also opportunity for firms to engage in cheap production technologies and expertise for a better asset combination. It has been proven that acquisitions have resulted to enhanced production as result of efficient management. The owners of firms to be acquired sell the stakes to

the acquirer as long as they feel they will gain and they are sure they may not achieve this by their own (Koller at el, 2010).

In the long run, the stakeholders of the acquiring firm expect huge benefits and hence they are willing to pay any price to acquire a target company. There has however, been a disagreement on a number of studies carried out since they indicate various beneficiaries on the acquisitions. Maditinos et al (2004) indicated that in the short run both parties do not gain but one party can only do so at the expense of the other parties. In recent past here in Kenya, there is an increased activity in the mergers and acquisitions. The takeovers are moving to the regions and we are seeing cross border acquisitions as well. Firms in the country are seeking to have a regional presence and hence increased need for acquisitions within the region and especially Kenya which the economic hub for the region (Maditinos et al 2004).

1.1.1 Evaluating Acquisition Success

The acquisition strategies do not have adequate insight from the empirical analysis. This has been the case due to many sizes and types of mergers and acquisitions and a there is no agreed method of grouping them by strategy. There has been however, various measures developed by financial economists to come up with a way of evaluating acquisition success of firms. The widely used is the one that happens up to around 11 days after acquisition announcement leading to changes in the company value. The financial economists evaluate the change of value of the acquiring firms as well as the acquired ones and finally the resultant one. In order to measure the success,

you cannot focus on either the acquirer or the target company. The correct way to do this evaluation is to ensure you measure the value of the combined firm. (Mitchell and Lehn 1990)

From an investor perspective overall it does not matter to the shareholders since their wealth will be maintained as much as this is the appropriate way to deal with this. The stakeholders or the owners of the companies should not worry much on events in the short run but the value of the new entity in the long run. The financial economists have come up with an evaluation of change of value the combined entity after announcement. When there is good information in the market during announcement, then we say then the change in value is appropriate. This information should be unanticipated and should only relate to the acquisition. It is said that, acquisition announcements return subsequently are informative as shown by empirical evidence. Kaplan (2002), suggested in his study that the subsequent success is linked and related to combined acquisition announcement returns. Mitchell and Lehn (1990) in the study done indicated that there is likely of a forceful takeover where the acquirers in acquisitions find that there are negative returns. In the recent past, Lehn and Zhao (2012) suggested that there is a likelihood that the top managent losing their jobs if the acquirers find the firm been acquired has negative returns. It is evident that all this studies indicate that returns on announcement will give useful information even if the R-squared is not one. (Lehn and Zhao 2012)

The experts in the long run have suggested that a change in value of the combined entity will take a period after acquisition three to five years. All the studies have made several crucial assumptions only the information about acquisition is available and hence the only factor shaping the price of acquisition. The financial economists have done studies using accounting over several years to measure financial performance using various ratios to determine the earnings of the firm as well as its cash flow. The same assumptions are made but with an additional one it comes to companies that are largely based on production where the change in productivity of the acquisition is usually determined by changes in level of firm's productivity (Kaplan 2002)

There is another category of study that determines the expected and the real change in value of the whole combination or merger. This studies will evaluate this by measuring expected and actual changes of the firm's value and cash flows. The studies will discount the expected cash follow to the present values so as to arrive at the present value of this companies. The studies would consider the period after equation and determine the cash flows changes to value and come up with this changes. There is a general assumption in the studies that the changes measures are expected and actual when it comes to acquisition.

1.1.2 Financial Performance

The general definition of Financial performance is the extent which financial objectives have been actually achieved. Actually it is the monetary terms of a firm expressed as expressed in terms of its results of its policies. Financial performance measures generally how the firm performs over a period of time. This is used also for comparison

of various firms in the same industry (Padachi, 2006). In order to create value of a company, there need to be a properly designed and implementable financial management policy (Padachi, 2006). The greatest challenge is to obtain the expected trade- off between earnings, solvency and liquidity (Lazaridis, 2006). Financial performance over the years has been a great area that many experts have been keen on and there has been numerous studies on the subject. This subject has been of interest to various parties form the business community, scholars, organizations and most importantly to any management that is focuses to have their firm's health improve over time. Good financial management policies will generally result to firms performing and hence there is proper utilization of company's resources which leads to improving the economy of a country (Naser and Mokhtar, 2004).

Financial performance can be measured using a number of ways. When you want to determine if an organization is using its assets optimally in its day to day running of its operations, we generally use the return on equity measure which gives how well the resources invested by shareholders are been used. The calculations that are used to measure financial performance have been generally agreed worldwide by the financial experts and are used to determine the success of firms (Tangen, 2003). There is also another measure that concentrates on the firm's ability to meet its financial obligations as they fall due in time, which is defined as Liquidity. There is operational liquidity which is generally the firms cash flow and the other type is the structural liquidity which is generally the linkage between assets and liabilities. When it comes to solvency of a firm, this is the measure of debts owed by a firm in relation to the shareholder's

equity. Solvency therefore gives an indication if the firm is in a position to settle all its debts if its assets were disposed. (Harrington and Wilson, 1989).

The firm's earnings or Profitability is another measure. This is actually a measure of a firm's ability to generate earnings as a results of the various investments in factor production which include management, capital and labor. This analysis concentrates around expenses and revenues of a firm and their relationships considering the size of the firm. In order to measure profitability, we use four measures which include; (ROE) return on equity, profit margin, (ROA) return on assets and net income (Hansen and Mowen, 2005). Another measure is the repayment capacity. This is the ability of a firms to settle its liabilities form operations as well as from non-operation income. Repayment capacity actually involves the ability of firms to service extra. There is no guarantee of future survival of a firm by the mere fact that in the short run, it has a positive cash flow (Jelic and Briston, 2001).

The financial efficiency can be said as how well a firm uses its factors of production labor, capital and management. When we talk of efficiency analysis we talk of the linkages between a firms output and inputs. Generally, fanacial measures are very possible due to the fact that we are able to measure inputs physical as well as in financial terms (Tangen, 2003).

1.1.3 Effect of Acquisitions on Financial Performance

The relationship between acquisitions and financial performance has been of great interest both to financial economists as well as scholars. There is great importance and what many studies have tried to explain is the various firm's performance and generally the types of investors and how they make choices when making such investments. The study on. To evaluate the problems or successes associated with performance after acquisition its pertinent to carry out on the effects of acquisitions on financial performance of a firms (Fabozzi, 1995).

Studies have found conflicting results of financial performance before and after acquisitions. Due to the different results as earlier explained, the question of the determinants of finance decisions in these acquisitions remains pertinent. There are those studies that indicate that after acquisition, there is great improvement in their financial performance (Azhagaiah and Kumar 2011). There has however some other studies that has indicated that after acquisition there is no financial benefits to the shareholders of the acquiring firms (Ndura, 2010).

In the short run, there owners of the firm been acquired will have great returns while on the other hand the shareholders of the acquiring firm will experience a drop in their share prices in the market into several months after the acquisition has happened with almost no overall gains in wealth. As explained in the differential efficiency theory, where firms that are not efficient enough and not utilizing their recourses optimally are likely to be potential targets by other firms that are more efficient firms. After acquisition, the combine firm according to the theory will operate more efficiently

more that the individual firms as they were before. This is evidenced by the new firm having economies of scale due to its size and hence it has better performance (Weston and Weaver, 2001)

1.1.4 Acquisitions Environment in Kenya

Wesonga (2006) indicated that in Kenya over the years especially until late 90s the economy had been dominated by state corporations and government and hence there were limitations to mergers and acquisitions in the country. There was pressure to liberalize economies and there was increased completion of firms due to globalization. Since this changes happened in the economy where most state firms were privatized and there was increased competition, we started seeing an increase in mergers and acquisitions in Kenya. In the year 1999 there were 24 acquisitions only as to compared to 1998 where there were about 23 (Cuts, 2002). The study points out that due to the bad performance of the Kenya economy then, many companies had to come together so that they could guarantee themselves a change into the future. There has also been new legal requirements especially on the minimum capital banks can hold and this has resulted the smaller banks merging in order to fulfill this statutory requirement issues by the Central Bank of Kenya.

Mwenda (2009), suggested his study that there were about 85 acquisitions which had been approved from 2002 to 2006. There creation of Competition authority of Kenya which replaced replace the Monopolies and Prices Commission. This was created by act of parliament known as The Competition Act (Cap 504). This change ensured that the new Authority was to deal with issues fair business practices in the economy and

ensure that it evaluated and approved all mergers and acquisitions in the country. The Competition Act (Cap 504) Section 27 outlined ways on determining if any acquisitions or mergers followed the correct procures and they are of public interest. The (CMA) Capital Markets Authority Act also is charged with regulation of mergers and acquisitions in Kenya especially for the firms that are listed in the NSE. The act is also very clear when it comes to procedures as well as timelines in which the mergers and acquisitions should happen.

1.2 Statement of the Problem

There has been increased acquisitions in recent past and it has become a very popular phenomenon. This has created a mixed reactions on the players as to the outcome of this acquisitions. There has been a number of studies both here in Kenya and the worls at large where there ther has been no agreement as to whether acquisitions improve the financial performance of acquiring firm's or not. There are studies that have shown that the financial performance of acquiring firms have improved there after acquisition (Kithinji, 2007: Azhagaiah and Kumar 2011: Korir, 2006: Ramaswany and Waegelein, 2003). On the other hand there has been some studies that have indicated that the acquiring firms do not have any financial benefits to them (Ndura, 2010). The firm been acquired in most cases in the short run have its stakeholders get good returns. The shareholders in the acquiring firms on the other hand may have some undervalued share price in the short run but with no overall wealth gains. There is also decreased EPS by the Acquiring firm's due to reduced earnings.

Empirically, studies have found conflicting results of financial performance before and after acquisitions. Due to the above varying results, the question of the determinants of finance decisions in these acquisitions remains pertinent. This study aimed to close the gap and give a clear picture on the impact of takeovers on the performance of the firms that acquire other firms.

Recently in Kenya (2014), Essar Capital, the fund manager of Essar Global Fund Limited, which through its portfolio company Essar Telecom Kenya Limited (ETKL), operated the popular yuMobile telecom service in Kenya, agreed to sell the company to Safaricom Ltd and Airtel Ltd for approximately US$ 120 Million in 2014. The divestment saw Safaricom take over ETKLs Network, its IT & Office infrastructure while Airtel Ltd acquired the subscribers. Against this backdrop, this study focuses on the effort to fill the existing research gap by determining the impact of YU Mobile acquisition on Safaricom Ltd and Airtel performance. The study therefore sought to answer the question; the impact of acquisitions on financial performance of firms in the telecommunication industry in Kenya.

1.3 Objective of the Study

The general objective of this study was to find out the impact of acquisitions on financial performance of firms in the telecommunication industry in Kenya

1.4 Value of the Study

The finding of this study is of great importance to corporate companies in Kenya as they gain knowledge on how the acquisitions create economic value. This information

assists various parties before they make any move to acquire another firm or accept an acquisition offer. With this knowledge, the investors can be able to predict firms' financial performance after acquisition which is an important fundamental variable in calculating firm's value and predicting stock prices.

This study is also valuable to academicians as it contributes to literature related to acquisitions. It assists students and other people researching on the acquisition and performance thereafter. This forms part of their literature review and can make reference and support their arguments.

To the shareholders the findings enable them to understand more about acquisitions, firm's value and firm's returns and how they are related and in turn affect each other. This helps them in making informed decisions as to accept an acquisition and the effect it has, what can erode or create wealth as a result of this.

Regulatory agencies such as NSE and Capital Market Authority (CMA) can use the study findings to regulate takeovers and mergers of organizations that are listed. The more the knowledge about a phenomenon one has the better equipped they are to face the challenges of the future. Effects of acquisitions, how it is affected by a firms return and how a change on it can affect the firm's value is a welcome weapon to facing the challenges of better management, and shareholder wealth maximization.

Though there have been some studies conducted on acquisitions, they have been inconclusive. Thus, this study is beneficial to the academicians in Kenya by narrowing the knowledge gap.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This section reviewed the existing theoretical and empirical literature. Section 2.2 is the theoretical literature review where various theories have been discussed. In section 2.3 Empirical Literature Review is on various empirical related studies on corporate mergers and acquisitions. In section 2.4 the determinants of financial performance are outlined.

The chapter finalizes by giving a summary of the literatures, empirical studies and the research gap.

2.2 Theoretical Literature Review

The theoretical section tried to uncover whether or not existing theories suggest that there is an impact of takeovers on performance.

The study adopted three main theories namely; Size and Return to Scale Theory, Differential Efficiency Theory and Inefficient Management Theory

2.2.1 Size and Return to Scale Theory

The size and return are crucial factors in this theory. This is the net gain or positive incremental as a result of with the combination of two firms through mergers or acquisitions. In an example when firm X acquires firm Z for cash. The total value

gained by the shareholders of X and Z is Synergy = VXZ - [VX + VZ]. If this results is positive, the combination of the firms (VXZ) is more valuable than the total of the other firms. From finance, the actual value of an asset is actually ist present value of the discounted Future cash flows. The cash flows in this case are: $\Delta CFt = CFABt - [CFAt + CFBt]$. When the results are positive, then the 2 firms result is greater cash flow than the of individual firms. Where there is no value created by the combination of X and Z, , then the combination is a zero-sum game. The economies of scale and the average costs decline with larger size. Large firms are abler to implement specialization.

In the study we seek to understand if Safaricom and Airtel operate more efficiently than the 3 firms individually. It is said in the theory firms can achieve a higher efficiency in a number of ways by a merger or an acquisition. The Economies of scale refers to the average cost per unit of producing goods or services. When per unit cost of production goes down for Airtel and Safariom as the level of production goes up, then we can say there is an economy of scale. According to the theory we also expect overheads to reduce and operational efficiency is improved since there is a sharing facilities acquired by the 2 firms.

2.2.2 Differential Efficiency Theory

Weston and Weaver (2001) proposes that there are organizations that are not operating optimally. The companies that operate in similar acuities are likely be the potential acquirers. These firms would have to detect the ones operating below average and have the management trained to improve of the performance of the acquired firm

This theory of differential Efficiency indicates that less efficient firms are acquired by the more efficient firms who will improve their efficiency. In the study Safariocm and Airtel are the more efficient firms and hence they acquired the less efficient firm Yu mobile. Inefficiencies in you mobile made it difficult to operate and compete effectively with other firms and hence the acquisition.

2.2.3 Inefficient Management Theory

In most cases the outcome of inefficient management is Mergers and acquisitions. This case is seen where the investors respond to case of inefficient policies by the current management resulting to a firm been an acquisition target by other firms (Asquith Bruner & Mullins, 1983).

Sugiarto (2000) suggests to identify inefficient management, there are certain indicators such as low price earnings ratio, low profit and share which are undervalued. Some of this factors are an indication of management that is not efficient and hence shows that the resources in this firms that are targeted are not efficiently utilized which encourages the takeover of such firms. The theory demonstrates that most likely Yu Moble had problems of management that resulted to poor performance. The enhanced earnings for Safariocm and Airtel on the other hand indicates efficient management and hence a response to acquire the less efficient firm which is Yu mobile.

2.3 Empirical Literature Review

Empirical studies on a number of mergers and acquisitions had their eyes on the effect of mergers and acquisitions on the firm's performance. This is because Mergers & Acquisitions are the common method of corporate strategy to improve firm performance. (Yeh and Hoshino, 2002) did a study on the the of mergers and acquisitions and their impact on company's overall performance especially on areas of profitability, the firms growth as well as how efficient they are. The major indicator of this study was the productivity of companies and hence the efficiency, ROA and equity There was a sample taken of 86 corporate mergers in Japan in the years 1970 to 1994. The outcome was that no much relationship between change in productivity. There was loss of jobs, low profitability, slow growth and less sales.

(Saboo and Gopi, 2007) embarked to find out how the performance of acquiring firms was affected by closely looking at various ratios before and after acquisitions and was able to compare the local and international mergers and acquisitions with cross border ones taking preference. The outcome showed that the effect or impact on the firms is significantly different for the local and international mergers. The findings also indicated acquisitions had a positive effect financial ratios of local mergers compared to international ones.

Andrade, Mitchell and Stafford (2001) explains on economics of acquisitions. They evaluated at mergers database at the Center for Research in the University of Chicago This data was for a period of twenty-five years. The outcome of this for the first 3 days

was the returns in the period was and statistically significant as well as positive. The resultant figures of the frim that acquired increased by 2% of value of acquiring firm and target firm. This shows that it is equal to an increase of about 10% of the target frim. The outcome is all the same in all years from the '70s to the '90s. Bruner (2004a) there are also many other surveys with the same outcome. The target firm’s returns are all positive. On the other hand, the acquirer’s returns are a little lower and negative, but not statistically different from zero. Over all the returns of both firms is positive. It is clear that one need not to evaluate the success of mergers by considering the target only or the acquirer since its likely to give misleading results. When a longer period is used to analyze this i.e. around 20 before the announcement until the acquisition closes, the resultant is the same, but they are not statistically significant.

It is true that acquisitions normally reveal some information not in the public on the 2 firms which is not related to the acquisition but will however affect the mind of the potential investors. This kind of information is crucial as it will affect the value of the stock prices in the market of the firm. It is important to be ready and know how to react to such. Mergers and acquisitions will normally combine investment decisions as well as financial ones. In most cases, the acquiring firm uses to the stock it owns to pay for an acquisition when she feels it’s stock is valued okay. In this case the interpretation of many people is that the firm asserts that their stock is overvalued. On the other hand the firm is less likely to use equity if there is undervaluation. It is common that firms that announce finance by equity without a merger have their stocks falling by about 3%. This finding show that the value of the acquirer – [AN-A0] – is in downward trend

when an acquiring firm utilizes equity to finance its acquisition. Acquisitions are in most cases a better measure of the average value of acquisition synergies.

Stafford (2001) suggests that mergers will have returns that are zero if funded by least some stock. On the other hand, any acquisitions that are not funded by the stock have positive returns combined.

In summary, studies show that announcement return is positive on average as viewed by the stakeholders. Consequently, the combined returns are positive for acquisitions that are not stock related and negative for the stock ones. There are sometimes negative estimates of value due to the information on the acquirer's value. The return announcement can be predicted and their outcome. The analyses sometimes may not be helpful due to the source of determinants of success.

Andrade, Mitchell and Stafford (2001) did a study on the same and focused on long run returns after number of years after acquisition. The outcome of the study was that the returns to acquiring firm are negative but statistically different from zero. Since the value of this acquisitions is huge they are open to scrutiny by the authorities. In the long run, the announcement return is a different between the stock acquisitions and non-stock ones. For the acquisitions that are not equity related, returns after acquisitions are positive and on the other hand the ones that are equity financed have negative returns.

Operating margins measures are used to evaluate the acquisition success as noted in the above. This results from the accounting-based studies have been used widely in many studies all over the world. Kaplan (2000) fount out neutral results in his study and on the other hand Ravenscraft and Scherer (1987) had negative results on the same subject. From all this studies, it is clear that the announcement return results vary depending on where you look at it. We are not certain that any acquisition can lead to productivity based improvements.

Schoar (2002) is his study suggests that the stand alone firms are less efficient than the more diversified ones. The organizations that get acquired are likely to have high production. The diversified acquire ring firms will push drive production and at the same time push the others to decline in productivity. The net effect is a decline in productivity in diversifying acquisitions. The ultimate outcome for all this studies is that there is no relationships between acquisitions and productivity performance. The explanation on this is that the data is not clean to filter the effects of the acquisition.

Locally, Kithinji (2007) did a study on the effects of acquisitions on financial performance of non-listed banks in Kenya. His sample was gotten form the years 1994 to 2001. A bank results analysis was done during the period before and after merger using various ratios. The outcome of this study showed that there was actually some improvement on the performance of this banks that had merged as compared to the others that had not merged. On the same note, locally Korir (2006) did a similar study on the effects of mergers and acquisitions on the performance of firms listed at the

NSE. He sampled 10 firms that has merged in the period of study. He also samples others that were not involved in acquisitions. The outcome showed an improvement in the financial performance of the firms that had merged.

In summary a number of empirical studies on various mergers and acquisitions had key interest on the effect of merger and acquisition on firm performance. The results clearly show the variations in terms of the impact on performance as a result of acquisitions considering if its local or international. The findings indicate acquisitions always have a positive effect on financial performance of local acquisitions more than that the international ones. Empirically, studies have found conflicting results of financial performance before and after acquisitions. With the many results of this, the question of the determinants of finance decisions in these acquisitions remains pertinent. This study aims to close this gap and give a clear picture on the impact of takeovers on the performance of the firms that acquire other firms.

2.4 Determinants of Financial Performance

This section reviewed and discussed the proposition and implication of research variables and how they affect the dependent variable. The study narrowed down the determinants of financial performance in takeovers and reviewed return of assets, return on equity, liquidity and other external factors. Profit is the main goal of every corporate organization. All policies and activities are designed to improve performance to achieve this goal. This however, does not mean that companies have no other goals. They also have more social and economic goals as well. However, the focus of this study is related to the objective of improved profitability. To measure the ultimate financial

performance companies in telecommunication industry, there are a number of ratios used of which Return on Asset and Return on Equity are the major ones (Murthy and Sree, 2003; Alexandru et al., 2008).

2.4.1 Return on Equity (ROE)

The financial ratio return on Equity is defined as the earnings of a company in terms of profit in relation to the total investors amount the total amount on the balance sheet. It is what the investors seek to have as a payoff of their investment. The firms with huge ROE are the ones that are able to produce much cash by themselves. It is the case that the companies with high ROE they are better in profit generation.

(Khrawish, 2011) explains that ROE is given by Net Income after Taxes / Total Equity Capital. This shows it is the return rate of the investments done by shareholders of a company. This ultimately is the a show of how effective a company utilizes the monies by the investors.

2.4.2 Return on Asset (ROA)

Another ratio that is of great importance is ROA. This is given by earnings of a firm. It is calculated as Income / Total Asset (Khrawish, 2011). It is a measure of the firm's capability generate income by using company assets by the management.

In addition, ROA shows how management is efficient in producing enhanced earnings from its resources. (Khrawish, 2011). (Wen, 2010), suggests that the more efficient firms are as a result of bigger and much higher return on assets.

2.4.3 Management Efficiency

One of the key factors that determine a firm's financial performance is Management Efficiency. It is shown by different financial ratios like total asset growth and profit growth. Financial ratios are a complicated subject but easy to interpret. Moreover, the efficiency of operations in managing the expenses is another dimension for firm's management quality check.

The management performance can be defined or explained through the evaluation of systems, the discipline the form, systems control, the staff, and others. Yet, some ratios of the financial statements act portray the management efficiency. The management ability to deploy the firm's resources efficiently, maximizing income, lowering expenses can be measured by ratios. The operational efficiency is greater when the higher the earrings to revenues of a firm id high. The ratio of management quality expense to asset is also very vital. (Athanasoglou et al. 2005).

2.4.4 Liquidity Management

The firm's financial performance is also determined by Liquidity. Liquidity is how a company is able to fulfill its obligations with ease. (Dang, 2011) suggests the acceptable liquidity level is linked with a firm's earnings positively. According to

Dang, the usual financial ratios that show the liquidity of companies are deposits of customers to total asset and to customer deposits on loans. There are other studies that have utilized other ratios as well. A good example of this is, (Ilhomovich, 2009) who utilized cash to deposit ratio to measure the liquidity level of banks in Malaysia.

Low liquidity assets in firms may result in selling of the company's investments in order to settle claims, this causes a decrease in performance due to losses incurred. The limitation of liquidity in determining performance does not necessarily involve firm's readiness to access to capital by current avenues of credit and other revolving agreements. It therefore cannot be used solely as a determinant of financial performance of organizations. Liquidity can be measured through percentage terms and absolute terms. The percentage measures examples of change in liquidity are working capital, current ratio, and quick ratio. Others where absolute measure of firm's liquidity is working capital, (Maina, 2014). The liquidity of a firm influences financial performance in that, a company with more liquid assets is able to release cash at any given time to meet its operation cost as and hence are exposed to few liquidity risks (Shiu, 2004).

2.4.5 External Factors/ Macroeconomic Factors

There are a number of external factors that affect the financial performance of a firm. Some of this factors which largely are macroeconomic include the political environment, prevailing interest rates, GDP and Inflation. The GDP flows influence demand for firm's asset.

When GDP growth is negative, the credit demand is low and hence affect profitability of this financial firms. On the other hand, when the GDP is growing, the credit demand for banks is high. It is the case that when we have a boom the demand for credit is higher than during recession (Athanasoglou and Brissimis, 2005).

2.5 Summary of Literature Review

The literature reviewed shows that there is an impact of performance of organizations after takeovers happens. The theories indicate that from acquisition the resulting company experience efficiency that I higher than the two original firms due to economies of scale as postulated by size and return to scale theory. Differential efficiency theory holds that the firms that operate with low efficiency and not optimally and are in the same business, they are potential targets for more efficient firms for acquisition. Firms mergers and acquisition is a response of inefficient operation and evidenced by inefficient management theory.

These studies indicate there is an impact of performance after a takeover however empirical studies have showed mixed results on this. The target companies generally have greater returns in the short run, on the other hand bidding firms will normally have a drop in their shares just after acquisition. The stakeholders of Acquiring firm's s may also have low earnings per share as a result of decreased earnings.

Profit is the major goal of almost all corporate organization. All policies and activates are designed to enhance and achieve this objective. It should also be noted that, firms may have other goals apart form profits. In the modern world, companies are engaging in corporate social responsibilities where they fulfill the social and economic goals. For the purpose of this study we focus on the profit objective. To establish the financial

performance of companies in the telecommunication industry in Kenya there are a number of ratios used and Return on Asset and Return on Equity are the major ones.

2.6 Conclusion

Various studies have found conflicting results of financial performance before and after acquisitions. Due to the various different results, the issue of the determinants of finance decisions in these acquisitions remains pertinent.

This study aims to close this gap and give a clear picture on the impact of takeovers on the performance of the firms that acquire other firms.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter outlined the methods that were deployed by the study in getting information on the impacts of acquisitions on the financial performance of firms in the telecommunication industry in Kenya

Section 3.2 outlined the research design giving the approach. Section 3.3 gave the target population of the study while section 3.3 is on Data and Data Collection Instruments used in the study. The final section which is 3.5 is on Data Analysis that was been divided into conceptual model and analytical model.

3.2 Research Design

A research design describes the scheme or plan of the general research approach adopted to a particular study. This research adopted a descriptive research design in order to determine the impacts of YU mobile acquisition on Safaricom Ltd and Airtel financial performance. By using a descriptive research design, the research was able to depict whether the acquisitions in the telecommunication industry in Kenya had an impact on the financial performance on these firms. Robson (2004) suggests that; descriptive research focusses on giving reliable results on variables so that there is better understanding of the study in question. Kothari (2004) agrees on this as well indicating descriptive research gives a framework for undertaking the social phenomenon, on the other hand Mugenda and Mugenda (2003) suggests that it gives a study the opportunity to show the various perspective to the variables. Therefore, the

survey was considered to be more efficient and economical. By using the descriptive statistics, the researchers will extract the average, standard deviation, observations for each variable to be used in the study.

3.3 Target Population and Sampling

The study target population represents the sum of the total variables of which are of interest to the study and of which have a very common characteristic as per (Mugenda and Mugenda, 2003). The target population under study consisted of Safaricom Ltd and Airtel Companies in Kenya.

The actual target population for this study comprised of finance departments of Safaricom and Airtel Kenya. Due to the target population being small, no sampling was done in the study.

3.4 Data and Data Collection Instruments

The study mainly used interviews as well as secondary data. This secondary data was gotten from the firms' annual published financial reports in data collection. The main reports of interest included; Statement of Financial Position, Income Statement, and Cash Flow Statement. The research used qualitative and quantitative methods both of which were used in data analysis.

According to Kothari (2008) both qualitative and quantitative aid in comprehending effectively the theme of the research since these methods complement each other. The collected data was recorded in Microsoft excel and the data analysis, it was done by Statistical Package for Social Sciences.

3.5 Data Analysis

We utilized regression model was used to determine the relationship between the variables. Data was analysed by Statistical Package for Social Science (SPSS Version 20.0) program. A multiple regression model was utilized to determine the impact of takeovers on performance. Below are the two major areas of data analysis namely conceptual model and analytical model.

3.5.1 Conceptual Model

The model takes the form of mathematical function:

$Y = f\ (X1, X2, X3, X4........)$ ....Equation (1)

Where:

Y= Dependent Variable i.e. Return on assets (ROA)

X1= Quick Ratio (QR)

X2= Current Ratio (CR)

X3= Total Asset Ratio (TAR)

X4= Debt /Equity ratio (D/E)

Based on the above regression model ROA becomes the dependent variable whereas current ratio, quick ratio, Total asset ratio and Debt equity ratio become the independent variables. The study Financial Performance is estimated by (ROA). Return on Assets is the measure of profitability in a number of studies. It indicates whether a firm is efficient in its management of assets to earn profit. The formula is as

follows: ROA = Net Income or Profit after Tax/Total Assets. The variable (X1) is Quick Ratio. Quick Ratio the other variable used to test for liquidity. It excludes stocks from current assets and hence a better variable. Stocks at tomes may be pilferaged or damaged or even suffer obsolescence. This shows whther a firm can to meet its short term obligations from its liquid assets. The acceptable bench mark for quick ratio is 1:1 and its formula is; QR = (Current Assets – Inventories/ Stocks) / Current Liabilities. The variable (X 2) is Current Ratio. Current Ratio is one of many measures of the financial performance of a firm's liquidity which is the safety level by the excess of current assets over current liabilities. The acceptable ratio for this is 2:1. And its obtained by dividing the current assets by the current liabilities that is; CR = Current Assets / Current Liabilities. The variable (X 3) is TAR. Total Asset Ratio is actually the net worth that a firm has in relation to its assets. You calculate this by; TAR = Net Worth / Total Assets. The variable (X 4) is the Total Debt Ratio. Total Debt Ratio is actually the proportion of liabilities a given company both short and long term liabities to its net worth. TDR is given as follows; TDR = Total Liabilities / Net Worth

These components in our model relates to the components that measure with financial performance of firms and assisted in determining if there is any impact of performance of Safaricom and Airtel after the takeover. The detail analysis was carried out with the help of above indicators. This study utilized regression coefficients to test the magnitude of the financial performance before and after the takeover.

3.5.2 Analytical Model

The general equation form of the of the multiple linear regression model used is as below;

$Yi = \beta 0 + \beta 1\ Xi, 1 + \beta 2\ Xi, 2 + \beta 3\ Xi, 3 + \beta 4\ Xi, 4 + \varepsilon$ ….Equation (2)

Where,

$\beta 1, \beta 2, \beta 3, \beta 4$= are the coefficient of independent variable

$\beta 0$= is the constant free term of the equation

E= is the error term of equation.

Xi = Independent variables

The research study was centered on its main goal by developing a financial model that was used to determine the relation existing in different indicators from the firm's financial statements which are shown through the financial performance. In other words, the analysis concentrated on the explaining financial performance especially on the carnages experienced by the firms in the current world. To be able to undertake this analysis of the research we utilized multiple linear regression method. To expound on this, the aim of adopting this regression is to clearly point out the relation between the independent and dependent variables. This multiple linear regressions, helps in a big way to explain partial or total variation of dependent variable as influence by independent.

3.5.3 Diagnostic Tests

The estimation methods to be utilized were financial ratio analysis method and in order to determine and test the correlation ratio between the dependent variable and each independent variable the Statistic-t test were going to be calculated as well as the probability associated to each combination of variables. This assisted in estimating parameters of the regression model and testing the level of significance.

This was by coming up with the coefficients of the regression model, standard errors, t test statistic value for each coefficient as well as value of the threshold of significance. Therefore, by analyzing the results from these findings of the t test and level of significance, it was possible to depict the relationship of financial performance based on mergers and acquisitions.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter gives the findings and outcomes of the study. The findings were presented to establish the impacts of the acquisitions on financial performance of firms in the telecommunication industry in Kenya.

The research used quantitative techniques in analyzing the data. After collectinon, the Secondary data was edited, classified, coded and tabulated to analyze quantitative data using Statistical Package for Social Science (SPSS) version 21.0.

4.1.1 Data Validity

The data validity indicates the extent to which the instrument measures the variables under investigation (Mugenda and Mugenda, 1999). It shows the degree to which a group of test things can be treated as measuring a single latent variable (Cronbach, 1951). Cronbach alpha was used to test if the instruments can be relied. This study considered a Cronbach alpha of 0.7 as the threshold for reliability. The Cronbach alpha in this case is from 0 – 1 and as it moves closer to 1, the more the consistency.

Table 4. 1: Test of Reliability and Validity

Variable	Cronbach alpa	Comment
Quick Ratio	0.733	Accepted
Current Ratio (CR)	0.891	Accepted
Total Asset Ratio	0.761	Accepted
Debt /Equity ratio	0.823	Accepted

Source: Research Findings 2016

4.2 Summary Statistics

Table 4.2 shows summary statistics for the study variables Quick Ratio, Current Ratio (CR), Total Asset Ratio and Debt /Equity ratio. The figures are tabulated from in terms of maximum, minimum and mean average as shown below.

Table 4. 2: Summary Statistic

	Minimum	Maximum	Mean
Quick Ratio	0.69	0.75	0.61
Current Ratio (CR)	0.71	0.75	0.62
Total Asset Ratio	0.14	0.25	0.19
Debt /Equity ratio	0.0	0.0	0.0

Source: Research Findings 2016

4.3 Impact of Acquisitions on Performance

The study focused on four variables that relate to performance of an institution these variables include Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR) and Debt /Equity ratio (D/E). These components in our model relates to the components that measure with financial performance of firms and assisted in determining if there is any impact of performance of Safaricom and Airtel after the takeover. The detail analysis was carried out with the aid of above indicators. This study used regression coefficients to test the magnitude of the financial performance before and after the takeover.

The study model further was used to answer to the following hypothesis

$H_{0:}$ Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR) and Debt /Equity ratio (D/E) do not have any relationship with financial performance of an institution

H_1: $H_{0:}$ Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR) and Debt /Equity ratio (D/E have relationship with financial performance of an institution

4.3.1 Results of Model Goodness of Fit Test

Table 4. 3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.973[a]		.943	.58162

a. Predictors: (Constant), Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio

(TAR), Debt /Equity ratio (D/E)

b. Return on assets (ROA)

Source: Research Findings 2016

The Coefficient of determination in this case gives the percentage of variation in the variables or the extent of which the dependent variable can be explained by the change in the independent variables (Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR), Debt /Equity ratio (D/E).

All the independent variables which were four in total, explain 94.6% of variance in Return on Assets shown by the R^2. This hence shows that other factors outside this this research contributed to 5.4% of variance in the dependent variable. Further research to this study should be conducted to determine the effect of external factors on financial performance of a firm.

4.3.2 Results of ANOVA

Table 4.4: ANOVA (Analysis of Variance)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	502.902	2	251.451	87.449	.000[b]
	Residual	28.754	10	2.8754		
	Total	531.656	12			

a. Predictors: (Constant), Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR), Debt /Equity ratio (D/E)

b. Return on assets (ROA)

Source: Research Findings 2016

The F critical at 5% level of significance was 5.21. This F calculated was greater than the F critical (value =87.499), this indicates that the model was significant. The significance is less than 0.05, this shows that the predictor variables), are able to give an explanation of the variation in the dependent variable which is Return on Asset. When the significance value of F is bigger than 0.05 then the independent variables do not explain the variation in the dependent variable.

Since the P value is less than 0.05 we reject Ho and conclude that Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR) and Debt /Equity ratio (D/E have relationship with financial performance of an institution

The findings above concur with the alternative hypothesis that the predictors i.e. Quick ratio, Current ratio, Total asset ratio and Debt to Equity ratio do have significant relationships with Return on Assets. Murthy and Sree (2003) indicated financial performance of an organization can be measured by a a variety of ratios of which Return on Asset and Return on Equity are the majority and directly impact on the financial performance of a firm.

4.3.3 Estimated Model

Table 4. 5: Coefficient of Determination

Model	T **B**	Sig.	
(Constant)	2.976	2.985	0.004
Quick ratio	0.877	3.286	0.001
Total asset ratio	0.588	5.796	0
Current ratio	0.705	2.796	0.006
Debt/Equity ratio	0.299	2.985	0.004

a. Predictors: (Constant), Quick Ratio (QR), Current Ratio (CR), Total Asset Ratio (TAR), Debt /Equity ratio (D/E)

b. Return on assets (ROA)

Source: Research Findings 2016

Which when the results are substituted to the equation,

$Y=2.976 + 0.8776X_i1 + 0.588X_{i,}2 + 0.705\ X_{i,}3 + 0.299\ X_{i,}3 + \varepsilon$

Where the dependent variable is Y (Return on Assets) X_i1 is Quick ratio, X_i2 is Total Asset ratio, X_i3 is Current ratio, and Xi4 is Debt/Equity ratio.

According to the equation, taking all factors (Quick ratio, Debt/Equity ratio, Current ratio and Total asset ratio) constant at zero, return on asset will be 2.976. The actual findings of the data also indicate that a unit increase in Quick ratio variable will lead to a 0.8776 increase in Return on asset; a unit increase in Total Asset ratio will lead to 0.588 increase in Return on asset; a unit increase in Current ratio will lead to a 0.705

increase in Return on asset; a unit increase in Debt/Equity ratio will lead to a .299 increase Return on asset.

The study findings are in line with literature review by Khrawish (2011) who found out that Return on Equity that determines how much profit a company earned compared to the amount of shareholder's equity invested. A business with high returns on Equity is more likely to have high profit generation.

Wen (2010) indicated in his study that if you have higher Return on Asset that indicates that company is efficient in utilizing its resources. Khrawish (2011) who defined Return on Assets as ratio of a company income to its absolute assets. He further stated that it's an indication of the way efficiently company's the resources are utilzed to generate the income.

Shiu (2004) argues that the liquidity of a firm influences financial performance in that, a company that has much liquid assets is in a position to release any amount of cash at any given time to meet its operation cost as and hence are exposed to few liquidity risks thus supports the findings.

The findings clearly show that Quick ratio has the biggest impact on financial performance of an acquiring firm followed by Quick ratio, Total asset ratio and Debt/Equity ratio.

4.4 Discussion of Findings

The independent variables that were studied in the research, explain 94.6% of variance in Return on Assets shown by the R^2. This is an indication that there are some other

external factors that contribute 5.4% of variance in the dependent variable. This hence is a confirmation that further research should be done to establish the effect of this factors on financial performance of a firm. 5% level of significance of F critical was 5.21. The outcome was that F calculated is higher than F critical (value =371.662), this was an indication the overall model was significant. On the other hand, significance is less than 0.05, hence showing that predictor variables), this was able to give an explanation of the variation in the dependent variable which is Return on Asset. When the significance value of F is larger than 0.05 the independent variables do not in any way show or explain variation. The findings above concur with the alternative hypothesis that the predictors' i.e. Quick ratio, Current ratio, Total asset ratio and Debt to Equity ratio have a significant relationship with the Return on Assets.

From the covariance matrix shown in the covariance matrix table; Quick ratio had a strong positive correlation (0.8776); this is interpreted that the current assets of the firm exceed the inventories of stock of the acquiring firm and therefore reflects a positive financial performance of a firm. Current ratio of the firm with a strong positive correlation of 0.705 indicates that the ratio of the firm current assents to current liabilities is positive and therefore is interpreted to mean strong financial performance. Total assets Ratio had a positive correlation of 0.588 and finally Debt/Equity ratio had a weak positive correlation of 0.299 are inferred to mean that Net worth of the firm is greater than total assets of the firm and the total liabilities outweigh the net worth of the firm respectively. The positive correlation of the variables indicates how they are influential in determining the financial performance of an acquiring firm

4.4 Summary

The findings above confirm the hypothesis that the independent variables Quick ratio, Current ratio, Total asset ratio and Debt/Equity ratio have a major relationship with the Return on Assets which is dependent variable. This means they directly impact on the financial performance of organizations.

The analysis also shows a positive correlation of the variables indicating that they are influential in determining the financial performance of an acquiring firm. Form the overall results it indicates that a business with huge returns on Equity is likely to have high profit.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMEDATIONS

5.1 Introduction

This chapter shows the findings of the study, data analysis and interpretation. It comprises of summary, conclusions and recommendations.

The study aimed to determine the impacts of acquisitions on financial performance of firms in the telecommunication industry in Kenya.

5.2 Summary of the Study

The outcome of the study found out that (R^2) which is the coefficient of determination and correlation coefficient which is (R) indicated the extent of association between Acquisition and Financial performance of a firm. The findings conquer with Azhagaiah and Kumar (2011) who concluded that indicate in the period after acquisition the acquiring forms have improved performance.

The study further found out that the significance value .000 which was less that 0.05 implying, the model was statistically significant in predicting Return on Asset. The results of statistical tests show that acquisition has a positive and significant effect on financial performance of an acquiring firm.

The study shows that Quick ratio with a strong positive correlation (0.8776) is interpreted as that the current assets of the firm exceed the inventories of stock of the acquiring firm and therefore reflects a positive financial performance of a firm. Current ratio of the firm with a strong positive correlation of 0.705 indicates that the ratio of the

firm current assents to current liabilities is positive and therefore is interpreted to mean strong financial performance. Total assets Ratio had a positive correlation of 0.588 and finally Debt/Equity ratio had a weak positive correlation of 0.299 are inferred to mean that Net worth of the firm is greater than total assets of the firm and the total liabilities outweigh the net worth of the firm respectively. The positive correlation of the variables indicates how they are influential in determining the financial performance of an acquiring firm

The study concludes that that positive Quick ratio, current ratio and Total asset ratio have a positive impact on Return on asset, however a positive Debt/Equity ratio negatively impacts financial performance but with a small magnitude.

5.3 Conclusion

According to the results of testing that has been done in chapter four it can be concluded that Quick ratio has a significant positive effect on Return on asset, and has a significant positive effect on firm' financial performance value.

The study further concludes that current ratio and Total Asset ratio affect the firm's financial performance

This study also concludes that acquisition of firms can also lead to an increase in liability of the firm that might exceed the net worth of the acquiring firm and hence leads to a positive increase of Total debt ratio that might affect the financial performance of the acquiring firm.

5.4 Limitation of the Study

The time available for the study was too short to adequately cover the research intensively

The cost of obtaining secondary data was high and some of the data was completely inaccessible to the researcher.

5.5 Policy Recommendations

The study recommends that during acquisition the acquiring firm should ensure that its current assets exceeds the total inventories on stocks

Further the study recommends that financial managers must ensure that the current assets of a firm and the net-worth of an acquiring firm tops the current liabilities and total assets respectively to maintain a steady financial performance of the firm

The study finally recommends that during acquisition the acquiring firm should ensure that the total liabilities should not exceed the net worth of the business by a bigger margin to mitigate on financial performance of an acquiring firm

5.6 Suggestion for Further Research

This study was carried to determine the impacts of acquisitions on financial performance of firms in the telecommunication industry in Kenya. Future research should strive to improve the identification of the linkages between financial performance of an acquiring firm and real variables such as environment and other external factors that might have a bearing on performance.

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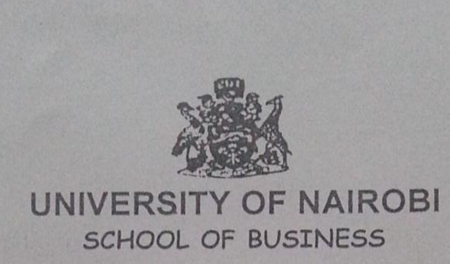
APPENDICES

Appendix 1: List of Firms to collect data from.

1. Safaricom Ltd

2. Airtel Kenya Limited

Appendix 2: Letter of Introduction



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TO WHOM IT MAY CONCERN

The bearer of this letter MARTIN MUNENE NJOROGE

Registration No. D61/67428/2013

is a bona fide continuing student in the Master of Business Administration (MBA) degree program in this University.

He/she is required to submit as part of his/her coursework assessment a research project report on a management problem. We would like the students to do their projects on real problems affecting firms in Kenya. We would, therefore, appreciate your assistance to enable him/her collect data in your organization.

The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

UNIVERSITY OF NAIROBI
23 SEP 2016
P.O. Box 30197 - 00100, NAIROBI

PATRICK NYABUTO
SENIOR ADMINISTRATIVE ASSISTANT
SCHOOL OF BUSINESS