EFFECTS OF MERGERS AND ACQUISITION ON THE FINANCIAL PERFORMANCE OF INSURANCE COMPANIES IN KENYA

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DECLARATION

I, the undersigned, declare that this is my original work and has not been presented to any institution or university other than the University of Nairobi for examination.

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LIST OF ABBREVIATIONS

AKI   Association of Kenya Insurers

CAPM Capital Asset Pricing Model

IRA   Insurance Regulatory Authority

M&A   Mergers and Acquisitions

NSE   Nairobi Securities Exchange

RBV   Resource Based View

ROA   Return on Assets

ROE   Return on Equity

SPSS   Statistical Package for Social Sciences

ABSTRACT

The objective of this study is to determine the effect of M & A on financial performance of insurance companies in Kenya. The study adopted descriptive cross-sectional design. The population of the study was made up of all the 12 insurance companies that had merged and/or had been acquired over the duration of 17 years between 2000 and 2016. The study used secondary data from financial statements of the merged companies before and after the merger. The pre and post M&A performance ratios was compared to see if there is any statistically significant change in value of the companies after M&A firms using paired sample t-test. Also Pearson Correlation coefficient test and regression was employed to assess the significance level. From the analysis of the companies' financial performance before and after merger, it was found that all the M & A resulted in an increase in financial performance after the merger. It also found that Pioneer Insurance, APA Insurance and UAP Insurance recorded the significant improvement in the profitability after merge and acquisition. Further, results shows that Metropolital Lite recorded a fairly high profitability ratio after merger while and UAP Old Mutual recorded a slightly small increase after merger. The profitability ratio for Saham dropped drastically after merger. The analysis of the companies' liquidity before and after merger showed that the average liquidity ratio for all the insurance firms increased after merger. The analysis of the companies' liquidity before and after merger showed that the average liquidity ratio for all the insurance companies except for Britam Insurance increased after merger. ICEA Lion posted the highest increase in liquidity after merger. This was followed closely by APA Insurance and Pioneer Insurance respectively. The results imply that merger and acquisition boosts the liquidity state of insurance firms. The analysis of the companies' total assets before and after merger showed that the average total assets increased for all the insurance firms post-merger. Results showed that UAP Insurance and UAP Old Mutual realized the highest increase in total assets after merger. This was followed closely by Britam Insurance. The results imply that firm size measured in total assets increases after merger. Further, the analysis of the companies' leverage revealed that the post-merger leverage was lowest in UAP Insurance followed by Pioneer Insurance. Results further showed that UAP Old Mutual, Saham and First assurance operated at highest leverage after merger. Less leveraged company attracts more investors than a more leveraged company. Regression results before and after merge and acquisition was presented. Before merge, profitability, firm size, liquidity, leverage had a positive and significant relationship with financial performance of insurance

companies. After post merge and acquisition regression results showed that profitability, firm size, liquidity, leverage the beta coefficients improved significantly. Model summary results indicated that value of R square before merger was 65.5 percent and 74.8% after merger. There was a significant change in R square before and after merge in indication of improved explanatory power of the predictor variables. From the study, insurance firms can improve their value by merging. By doing so the firms can identify synergies arising from economies of scale, increasing efficiency and diversifying risks. Through merge and acquisition, insurance firms can increase their asset base which will boost their competiveness in the market place. They are also able to minimize liabilities by reducing the debt equity ratio. Large organizations are able to access financial resources at a lower cost as well. Large corporations also diversify their assumed risks effectively and respond more quickly to changes in the operating environment and market. The Insurance Regulatory Authority may find it useful when recommending for M & A, their positive impacts and /or their negatives effects to the performance of the firms involved.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The modern day business environment has undergone evolution which has necessitated the businesses to re-evaluate their strategies in order to remain competitive and relevant. As such, different companies have taken different strategies in order to fit in the ever changing environment. Mergers and acquisition has become a common activity among many companies around the world. Research done on relationship between mergers and acquisition and financial performance has created a debate on increase on value of the target firm and not the acquiring firm whereas other researchers argue that it increases the value acquiring firm especially in the long run (Twan, 2012) while others argue the there is an increase in value of both acquiring and target firm .Mergers and Acquisition is an external corporate restructuring which can be simply defined as a legal consolidation of two entities into one (Emy & Hamza, 2016). In specific terms, a merger is a situation where two companies come together and form one large company, while Acquisition is where one company buys a controlling stake in another company (Stunda, 2014). M & A had become a nearly every day affair in the business environment with the main objective being to maximize shareholders' wealth. However, some M & A are necessitated by other factors such as regulatory requirements and as such, may not necessarily lead to shareholders' wealth maximization.

There have been various theories which explain the need for M & A as a solution to the different challenges facing the business environment. This study focused on the three studies, that is, efficiency theory, agency theory and hubris theory. Efficiency theory which explains that through M & A a firm is able to transfer its superior operational, financial or managerial efficiency to the other combining firms. The increased efficiency will in-turn ensures that the value of the firm is maximized. Another theory is the agency theory which states that there exist a conflict of interest between managers and shareholders. The agency theory states that the managers are expected to make decisions which are in line with the shareholders' wealth maximization. However, this is never always the case since the managers have conflicting goals and aspirations. As such, shareholders will inevitably undertake activities which favor their interests much as this may not necessarily be in the best interest of the managers. A company which is being acquired may lay off its managers or reallocate them to seemingly inferior roles

but eventually the shareholders of the acquired company end up getting a high value for their shares. This theory was advanced by Roll (1986) and argues that managers often fail in evaluating merger feasibility due to excessive self-confidence leading to errors of optimism.

Mergers and acquisition has been happening in the Kenyan insurance industry since early 90s. The most recent merger has been UAP-Old Mutual Group, where UAP Holdings agreed to merge with Old Mutual group to form one entity in June 2015. Financial performances for merged insurance companies have been of great interest to researcher. Some studies done have concluded that M & A have improved financial performance of the post-merger firms (Mwanza, 2016).

1.1.1 M & A

M & A (M&A) is a term commonly used to refer to the legal union or combination of companies so that they operate as a single entity. According to Cartwright and Schoenberg (2006), A merger is the amalgamation of two existing companies to bring forth a new company where the joint firms retains their identity while an acquisition is taking control of a company by purchasing most of the company's ownership stake with no new company being formed. However, Berkovitch and Khanna (1991) argue that a merger, an acquisition and a takeover have a similar meaning. They all mean an offer which is made by the bidding firms to the shareholders of target firms. There are other varied ways in which one company can acquire another among them is buying a company's outstanding shares of stock or purchasing a company's assets (DePamphilis, 2008).

M & A take place in three key forms; horizontal mergers, vertical mergers and conglomerate mergers. The horizontal form of merger takes place in firms that operate in the same industry; usually competitors offering similar goods or services (Martin, 2015). Marembo (2012) defines horizontal mergers as the acquisition of competitors in the same business line in order to increase market share and reduce competition in one strike. Vertical mergers on the other hand take place among business entities producing totally different goods or services that are input into the process of producing another product (David, 2009). Finally, conglomerate mergers occur between firms that produce unrelated products (Halpern, 1983).

Different organizations are faced with different motivations for M&A. The main motivations advanced for M & A are: gaining market power, enhance innovation, and hence minimize

product development risks, efficiency maximization via economies of large scale production and reshaping a business' competitive scope (Hitt, Harrison & Ireland, 2009). Other factors in favor of M & A include providing short-term financing solutions to challenges arising out of information asymmetries, revitalize the company through knowledge and skills necessary for survival in the long term and to benefit from synergies.

1.1.2 Financial Performance

The extent to which the firm's financial objectives have been attained is described as financial performance (Yahaya & Lamidi, 2015). The financial performance of a company defines the firm's efficiency in utilizing its assets to undertake various business activities so as to generate revenues. Financial performance also shows the firm's general well-being with regards to financial stability. The competitiveness of a firm could also be gauged by comparing its financial performance with those of others across the same industry. Financial performance is, in summary, is a crucial objective that firms especially the profit oriented firms desire or aim at to achieve (Kajirwa, 2015).

Institution effectiveness is measured by firm performance and its capacity to accomplish its objectives as far as profits and revenues are concerned (Ongore and Kusa, 2013).Financial performance affect the health of the organization and its overall survival in the long run. High performance is an indicator of the effectiveness and efficiency of the management in utilizing the resources of the company which is detrimental to the economy in the long run (Naser and Mokhtar, 2004).Financial performance provides financial information to the various administrative levels of unity for the purposes of economic planning, control and decision-making.

Financial performance can be measured using different techniques which must all be consolidated. Ngatia,(2012) identified ROE (ROA),asset age, firm size, Return on Equity (ROE) and return on sales as micro finance performance measures. Carter *et.al* (2010) measured financial performance using Tobin's Q and ROA whereas Wang and Clift (2009) used ROA and ROE. The two most well-known measures of productivity are ROA and ROE; hence, this study will compute the financial performance of publicly listed companies using the two measures. ROA shows the company's profitability is in relation to its total assets and ROE measured the net income attained as a percentage of equity of the shareholders. It measures the profitability of the company the amount of profit generated through utilization of company resources. ROE is useful for comparison of the firm's profitability with those of others in the same sector. High ROE implies that the firm is efficient the firm is making use of those funds (Mwangi & Murigu, 2015).

1.1.3 Mergers & Acquisitions and Financial Performance

Research reveals that there is a great degree of variance on the association between M & A and the financial institutions' financial performance. For instance, Rhoades (1998) asserts that M & A can lead to significant cost reductions that can enhance financial performance of financial institutions whereas for other institutions it may not lead to cost reductions. Sufian and Abdul Majid (2007) also argue that M & A lead to enhanced profitability but have a negative side such as creation of monopolies and synergies.

A study by Girma, Thompson and Wright (2011) indicated there was a rise iof £300-400 in the average operating profit per employee of the acquiring firms three and four years after being acquired, this is a good indicator that could be adopted. They investigated this effect further by balancing other forms of acquisition. These results revealed that although both merger types positively affect profits, the magnitude and timing of these effects differs. Based on these researches therefore, we can infer that mergers and acquisition would positively impact financial performance of an organization.

Heron and Lie (2002) noted that the financial performance of firms improved after a combination; specifically, the firms studied experienced improved asset turnover and reduction in capital expenditure. Fatima and Shehzad (2014) on the other hand revealed that there was no significant relationship in the ratios of commercial banks pre-merger and post-merger; and thus reached a conclusion that mergers did not lead to the improvement of the financial performance of Banks. Quite a number of organizations are involved in M&A's so as to enhance their value and they are an effective way of improving the performance of corporations through increase in revenues and profitability. M&A's enhance growth through increase in the market share and creation of synergies for organizations.

1.1.4 Insurance Companies in Kenya

The Kenyan insurance industry is among the most vibrant insurance markets in Africa in terms of performance, penetration and growth potential. The Kenya insurance sector has 49 insurance companies, 3 reinsurance companies, 204 insurance brokers a, 10 reinsurance brokers 7720 insurance agents in Kenya. 24 companies offer non-life insurance business only, 13 specializes in life insurance business while 12 are offer composite insurance products (both life and non-life) (IRA, 2016). Ten insurance firms are listed on the main investment segment of the NSE

(NSE, 2017). The government established the Insurance Regulatory Authority under the insurance act CAP 487 to supervise and develop the Kenya's insurance sector (IRA, 2018).

Strategic acquisitions have become a commonality in Kenya's insurance market. The common M&A include Lion of Kenya Insurance Company and Insurance Company of East Africa to form ICEA LION Group, the merger of Apollo Insurance Company Ltd, and Pan Africa Insurance Company to form APA Insurance. Intense competition and desire to increase efficiency has forced the insurance companies to pursue more the middle class who are seeking high returns and high returns. The growth of the oil and gas sector has attracted international investors into the Kenyan market leading to strategic alliances so as to serve these bigger companies (Kenya Insurance Industry Report, 2016).

The insurance sector recorded a 13.4% growth in gross written premium of Ksh197.0 billion in 2017 up from Ksh173.79 billion in 2016. Gross earned premium increased by 10.9% to stand at Ksh161.15 billion in 2017 compared to Ksh145.27 billion in 2016. The industry recorded a profit of Ksh15.47 billion before tax in 2017 compared to Ksh10.86 billion in 2016. The industry asset base in 2017 grew by 9.0% to stand at Ksh508.18 billion compared to Ksh466.36 billion in 2016. In 2017, the overall insurance issuance was 2.75% compared to 2.78% in 2016. The World average insurance penetration in 2017 was 6.0%. The sector aims to attain 6.0% penetration level by 2020 tapping into opportunities that exist for insurance business in areas such including gas and oil, infrastructure, real estate, bancassurance, agriculture and micro-insurance (AKI, 2017).

1.2 Research Problem

The concept of the effect of M & A on companies' financial performance is an area of great concern to many scholars and various stakeholders because financial performance is a critical measure of the general performance of any organization. It is assumed that the value of the merged firms in consolidation is higher than individual firms operating as standalone. Most research in the past concluded that M&A announcements enhances significant positive returns for target firm's shareholders but have negative or zero returns of bidding firms' shareholders owing to the fact that bidder companies pay a premium to the target companies. This argument has been challenged over the years (Fluck & Lynch, 1998).

The insurance sector in Kenya has over the recent past experienced several M & A. This can be mainly attributed to the changes in the regulations in the insurance act which required insurance companies to double their minimum capital requirements to Ksh. 600 million up from Ksh.300 million for short-term insurers and ksh.400 million up from ksh. 150 million for long term insurers. With the IRS introduced a new phenomemon of risk supervision, risk based capital adequacy is also a requirement. Insurance companies have been given up to the year 2018 to comply with these new requirements (IRA, 2017). Those who are not able to increase their capital will be forced to merge or be taken over by bigger companies.

Several studies have been done in the area of M&A's and they have yielded mixed and inconclusive results on the effects of M&A's on the financial performance of an organization. Friesen (2005) study on the effect of a horizontal merger announcement between Air France and KLM found that Air France shareholders as the bidder firm experienced insignificant returns whereas KLM shareholders experienced significant positive abnormal returns. Ward and Smit (2007) did a research to determine whether large acquisitions add value to acquiring companies quoted on the Johannesburg Stock Exchange Limited. The conclusion of the study was that large acquisitions generally give a zero NPV investments for acquiring companies and the shareholders. This study contradicted with that of Liang (2013) who found that bidding firms received a significant and positive abnormal return. Khanal, Mishra and Mottaleb (2014) results also showed cumulative average abnormal returns of the bidding firms.

Locally, Marembo (2012) examined the impact of M & A on commercial banks' financial performance and noted that M& A did not enable the banks to attain strong, competitive and efficient markets since several factors determined performance. However, a solution to this study was provided by Marangu (2007) who argued that that significant performance improvement of the non-quoted insurance firms were attributed to merging as opposed to the non-quoted insurance companies that had not merged within this time span. Kiprotich (2017) studied the relationship between M & A on value of listed insurance companies and concluded that mergers and acquisition have a positive but not statistically significant relationship with firm value. Mwanza (2016) carried a study on the effect of M & A on financial performance of Kenyan insurance companies. The conclusion from the study was that M&A enhance the financial performance of the merged firms. However, the study by Mwanza (2016) considered two year pre-merger and post-merger financial performance data which may be too short for one to observe the financial performance of a firm and make conclusions. This study therefore seeks to establish whether M&A have any impact on financial performance of insurance

companies by taking a longer duration of study. This study seeks to answer this research question: Do M&A have an effect on financial performance of insurance companies in Kenya??

1.3 Objective of the Study

To determine the effect of M & A on financial performance of insurance companies in Kenya

1.4 Value of the Study

This study's findings may be used as a reference by scholars, students and researchers who might want to undertake studies in the same field. The study may also help both researchers and scholars in identifying research gap in this field which may prompt and guide them in executing further studies.

The study may help the management update themselves on the current industry practices because of the very dynamic nature of the business environment in which the organizations are a part of. It may assist both the management and the shareholders with information that may assist in predicting and ensuring good timing for the M&A's.

This study may also be of importance to the regulator, Insurance Regulatory Authority (IRA) in understanding the best ways to mitigate risks and in coming up with appropriate regulations. This may guide the government on matters pertaining to regulation on M & A and making policies related to M&A. The study may also be of great value to Kenyan Insurance firms that intend to adopt M&A as a means to growth and profitability by giving empirical evidence of M&A on profitability.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter reviews theories that form the foundation of this study. In addition, previous empirical studies that have been carried before on this research topic and related areas are also discussed. The other sections of this chapter include determinants of financial performance, conceptual framework showing the relationship between study variables and a literature review summary.

2.2 Theoretical Framework

The concept of mergers and acquisition and its relationship with financial performance is explained by a number of theories. In this study, three theories have been discussed which include; efficiency theory, agency theory and the hubris theory.

2.2.1 Efficiency Theory

The efficiency theory was advanced by Banerjee and Eckard (1998) and it argues that, mergers only take place if its subsequent benefits will be valuable to the two parties involved. There are types of synergies that likely to be accrued due to mergers. These include; the financial synergies which are realized through lower costs of capital since mergers lower the systematic risk of the investment portfolio of the company through diversification into other lines off business. The second technique is by increasing the size of the company thus increasing access to cheap capital. The third synergy is the establishment of an internal capital market due to open access to more superior information thus increased efficiency in capital allocation.

According to Porter, (1985), operational synergies also arise through combination of operations of two independent units for instance joint sales force or knowledge transfers. These two forms of operational synergies reduce the cost of that could have been incurred by the two business thus enabling the company to offer differentiated goods and services. However, all the potential advantages must be compared against the associated costs of the merger and asset transfers.

According to Jensen & Murphy (1988), positive motivation are associated with LBOs. Many criticisms have however been advanced against financial synergies with the main one being

that they cannot exist in efficient capital markets. Other studies have demonstrated that evidence lack on superior internal capital market and lower systematic risk (Montgomery & Singh, 1984; Rumelt, 1986). The efficient theory was useful in ascertaining the synergies associated with the mergers and acquisition processes.

2.2.2 Agency Theory

This theory was propelled by Jensen and Meckling in 1976 but originated from the work of Berle and Means (1932). Under this theory, managers are seen to be self-centered and will only carry out the process of M&A if it contributes to their personal wealth (Agrawal & Knoeber, 1998; Ghosh &Ruland, 1998). These objectives do not necessarily maximise shareholder returns (Firth, 1980). The Agency theory is harmonious with the argument of Larcker (1983) who states that managers concentrate on the decisions that are short term in nature and try to maximise the available firm resources within the limited time frame. Again, this argument is reasonable because most managers are employed for a short span and consequently they will try to maximise their personal wealth before the termination of their contract. On the other hand, shareholders prefer maximization of their return. To minimize this agency problem between the management and shareholders, it is imperative for companies to provide their managers with incentives such as share options.

On the issue of incentives, some studies argue that acquiring firm managers with personal wealth that is more linked to the value of the firm make better acquisition decisions. For example, Tehranian, Waegelein and Travlos (1987) indicated that acquirers that own long-term compensation plan are more active than those with short term plans. Further, Raman and Datta (2001) reveal that managers with more equity-based compensation make better acquisition decisions. Furthermore, Lewellen, Rosenfeld and Loderer (1985) purport that firms with high managerial stock ownership possess higher acquirer returns.

On the aspect of monitoring, evidence reveal that more intensive supervision of managerial actions through board of directors, leads to better acquisition decisions. Byrd and Hickman (1992) explore public firms' tender offers and the findings reveal that acquirer returns rise with the extent of outsiders constituted in the board. However, Masulis, Xie and Wang (2007) dispute this association, while Stegemoller and Bauguess (2008) purport that a negative link exist as evidenced by S&P 500 (large) acquirers.

The relevance of this theory is that it tries to explain M&A as a shared goal that serves to align the interests of shareholders to that of managers. Managers conduct M&A if they contribute to their personal wealth. Acquiring managers whose personal wealth is closely linked to firm value make better acquisition decisions. In order for M&A to enhance shareholder returns, managers can be compensated based on stock price changes and performance based incentive plans such as managerial stock ownership. Monitoring is also relevant by intervention of shareholders through representatives in the board.

2.2.3 Hubris Theory

This theory was advanced by Roll (1986) and argues that managers often fail in evaluating merger feasibility due to excessive self-confidence leading to errors of optimism. Rational bidders are always careful in developing anticipated merger returns so that the actual project values do not fall below the projected ones. Therefore, managerial motives are vital determinants for M & A outcomes as managers may be motivated to build bigger empires due to their vested utility (Zalewski: 2001; Trautwein: 1990) as opposed to the value of the shareholders. Jensen (1988; 1986) purports that managers could invest the free cash flow in acquisitions projects with negative NPV if it results to higher personal utility instead of maximizing the shareholder value. The free cash flows that are present in the reserves must be issued to the shareholders as dividends in order to increase the firm's efficiency and increase the stock prices (Jensen, 1986).

According to (1989), managers in conglomerate mergers experience employment risk since their future potential with regards to employment and earnings are highly linked to the risk level of the firm. Consequently, the risk averse managers get into M&A as a cover against employment risk as opposed to the shareholders' benefits since such forms of risk are not diversifiable in their own portfolio.

Mueller (1969) advanced a model for growth maximization for M & A anchored on the perspective that the manager's social status, bonuses, promotions and salary are related to firm size. He proposes that due to this association, managers easily for ROI that is lower than the requirements of the shareholders. Therefore, managerial hubris is cold be defined as an agency problem brought about by the separation of ownership and control leading to disputing interests between the managers and shareholders.

Ephirical studies have been undertaken to determine whether the manager's actions strive to maximize their own actions or the shareholder's. A study by Lewellen and Rosenfield (1985) explored 191 acquiring firms' stock returns between the time frame 1963 -1981 and the findings revealed that a strong positive association exists between abnormal stock returns from M&A and the extent of management ownership of the acquiring firm. A similar study by Firth (1991) tested the association between executive rewards and M&A. The findings revealed that an increment in the shareholder value goes hand in hand with an increment in the executive rewards. However, even if the shareholder wealth is destroyed, executive remains to gain from the M&A. The theory shows how M& A influence the firms' share value.

2.3 Determinants of Financial Performance

There are a number of determinants of performance in companies. These factors usually cut across almost all the sectors in the economy. They include M & A, company's liquidity position, management efficiency, financial leverage, firm size and macro-economic variables.

2.3.1 M & A

M & A is an easier way that could be adopted by firms to broaden their product portfolio, increase their scale of their operations and enter to new markets. The motive for undertaking M & A activities is to enhance value for the shareholders by increasing their value. In 2001, a study shows that 20 of the companies in the population failed due to poor management of the merged companies (Boot, 2011). The financial position of the firm is important in ascertaining whether a firm should engage in M&A acquisition. A firm only engages in M&A only if it will accrue benefits from the merger (Andrade, 2004).

Acquisitions and mergers enable competition elimination and protection of the existing markets through new market outlets acquirement (Bloom, Sadun, & Van Reenen, 2012). This is by use of market power where one firm acquires another to increase its market power and share market. Profits are enhanced in such mergers through reduced competition and high prices. Product and service diversification: Another reason for company mergers is for current service or product complementation. Products or services can be combined by two firms to attain a competitive edge against other market players (Wright, 2011). Regarding economies of scale, Acquisitions and Mergers translate to the a boost in the purchasing power in the acquiring of office equipment supplies in larger orders placement, companies can easily negotiate for prices with their suppliers. Improved industry visibility and market reach where companies easily

merge to capture new markets and easily grow earnings and revenues (Sufian & Habibullah, 2009).

2.3.2 Liquidity

Liquidity is defined as the degree in which an entity is able to honor debt obligations falling due in the next twelve months through cash or cash equivalents for example assets that are short term can be quickly converted into cash. Liquidity results from the managers' ability to fulfill their commitments that fall due to policy holders as well as other creditors without having to increase profits from activities such as underwriting and investment and as well as their ability to liquidate financial assets (Adam & Buckle, 2003).

According to Liargovas and Skandalis (2008), liquid assets can be used by firms for purposes of financing their activities and investments in instances where the external finance is not forthcoming.).Firms with higher liquidity are able to deal with unexpected or unforeseen contingencies as well as cope with its obligations that fall due in low earnings period. Almajali et al., (2012) noted that firm's liquidity may have impact on insurance companies' financial performance; therefore he suggested that insurance companies should aim at increasing their current assets while decreasing their current liabilities. However, Jovanic (1982) noted that an abundance of liquidity may at times result to more harm. He therefore concludes that the effect of liquidity on firm's financial performance is ambiguous.

2.3.3 Management Efficiency

Management efficiency is a key internal factor that qualitatively measures and determines the financial performance of a firm. The ability of the management to efficiently utilize the resources of the firm, their ability to maximize revenue and their ability to reduce the cost of operation of the firm are some of the ways of assessing the management quality. Management efficiency is a qualitative measure and determinant of financial performance and it can be assessed by looking at the quality of the staff, the effectives and efficiency of the internal controls, the discipline within the organization and the effectiveness of the management systems (Athanasoglou, Sophocles & Matthaois, 2009). The quality of the management has an influence on the level of operating expenses which affects the bottom line of a company hence management efficiency significantly affects the financial performance of commercial banks (Kusa & Ongore, 2013).

2.3.4 Capital Structure

Capital structure is also another important determinant of financial performance of a firm. Every industry needs a substantial amount of resources, be it land, labor or capital employment of all finances required. These finances are either internally or externally generated. The sources of finance are selected based on their associated costs and the firm's capital structure. These can either be monetary or nonmonetary costs. The firm's performance is highly determined by its capital structure. The firm's debt to equity financing is defined as its capital structure. According to Su & Vo, (2010), more debt financing puts the company under bankruptcy risk. However, debt financing is also associated with some monitoring and tax benefits and combats the agency conflict through reduction of the firm's free cash flow. Abu-Rub, (2012) opines that the firm should operate under a suitable capital structure that generates the optimum profit for the companies since less equity financing increase the owners' control to a large extent.

2.3.5 Firm Size

Burca and Batrinca (2014) asserts that the relationship existing between size and financial performance is positive in the sense that more resources are available in larger firms, better risk diversification strategies, complex information systems and are able to manage expenses well compared to small firms. This may have an impact on the financial performance of insurance companies in different ways for example large firms may be advantaged compared to smaller firms as they can be able to exploit economies of scale and scope and as such they are more efficient in their operations and as a result reap higher level of profits.

According to Almajali et al., (2012) the firm's size may have an impact on its financial performance. The relationship between performance and size is positive due to the fact that there are efficiencies in operating cost that result to increased output and economies of scale. Insurers of large companies are able to diversify their risks hence are able to quickly respond to any changes that may occur in the market. Yuqi (2007) noted that in firms that are exceptionally large, there could be a negative performance in relation to its size due to bureaucratic and other costs implications.

2.3.6 Age of the Firm

According to Sorensen and Stuart (2000), company's age may have an effect on firms' performance. They further noted that older firms may have organizational inertia which tends to make them inflexible which may result to their inability to appreciate the changes that occurring in changing environment. However, Liargovas and Skandalis (2008), noted that older firms may have more skills because they have been in operation longer thus have more experience having enjoyed the benefits that come from learning and aren't prone easily to the liabilities that result from newness therefore they tend to have performance that is superior as compared to newer firms.

According to Loderer and Waelchli (2009), the relationship that exists between the age of a company and profitability is positive. However it has also been observed that firms performance may at times decline as companies grow older due to the fact that old age may lead to knowledge, abilities and skills being obsolete thereby resulting to decay in organizations. Agarwal and Gort (2002) this may explain why some older companies are usually taken over.

2.3.7 Macro-economic Factors

A number of studies have been undertaken to determine the effect of macroeconomic factors on performance of companies. The factors include but not limited to monetary aggregates, rate of interest, investment level in the economy, consumer price index, producer price index, GDP growth, inflation, financial depth and the degree of market efficiency. Kwon and Song (2011) carried out a research on mergers the Korean market. He found out that the global financial crisis has a significant negative effect on the cumulative abnormal returns of the acquiring company when a merger announcement is made. He also stated that it may be possible that investors are aversive to large outflows of cash during a period of crisis. Flannery and Protopapadakis (2002) pointed out that inflation and money supply are well documented as the two macro-economic factors that have a significant effect on shareholders returns.

2.4 Empirical Review

A number of empirical studies have been conducted both locally and internationally to support the relationship between M & A and financial performance, but these studies have produced mixed results.

2.4.1 Global Studies

Adebayo and Olalekan (2012) studied the implication of M&A's on the profitability and other performance measures on commercial banks in Nigeria by looking at 10 commercial banks that emerged from the consolidation in 2006 through a survey study. They used a simple percentage for the analysis and tested hypotheses using correlation coefficient and t-test. The study found that there was a significant relationship between the capital base of the commercial banks and their profitability before the merger and after the merger. Further, they found out that M&A's led to the increased capitalization of commercial banks which was confirmed by the changes in the ownership structure, changes in the lending rates of the banks and the increase in the cost of the services offered by the banks. However, the study found out that there was significant difference in the Earnings per Share (EPS) before the merger and after the merger. They concluded that the M&A's programme led to the growth of the real sector for sustainable development to a great extent.

Liang (2013) also looked at impact of M&A announcement of domestic and cross border firms listed in the Hong Kong stock market over the period of 2007- 2012. He examined whether the M&A announcement have been creating or reducing wealth for the shareholders of the acquiring firms. Using the event study methodology as a method of analysis, the researcher found out that the acquiring firms indeed received significant positive abnormal return. He concluded that the market expectation is main determinant of the impact of M&A announcement on stock price movements.

A study by Fatima and Shehzad (2014) looked into the impact of M&A on Pakistan insurance companies' financial performance by analyzing six financial ratios. The sample of the study was ten selected insurance industries that were involved in mergers between the time frame 2007 and 2010. The study took data points of 3 year pre and post -merger of all the 10 cases selected and a comparison of their averages undertaken. The study's null hypothesis was Ho; M & A increase the firm's profitability and efficiency by way of synergy while the alternative implicated that M&A had a negligible effect on financial performance. From the results, the

alternative hypothesis was rejected with regards to profit after tax, leverage, earnings per share and ROE while the null hypothesis was accepted. The study concluded that mergers' objectives were not clearly obtained, economies of scale were not achieved neither was synergy created.

Khanal, Mottaleb and Mishra (2014) used an event studies to examine the recent M&A announcement on the stock prices and firm value of publicly traded ethanol-based bio fuel industry over the period of 2010 and 2012 in the United Sates. The findings showed positive average cumulative abnormal returns of acquiring firms meaning that the market responded positively toward recent M&A in the industry. Evren and Ali (2015) investigated the reaction of target firms' stock returns in M&A announcements of twenty markets are emerging. Using the event study for a sample of 1,648 M&As' between 1997 and 2013, they found out that announcements of M&A generated a 5.17% average abnormal return of the stock of the target firm within event window of three days.

Masud (2015) studied the impact the impact of M & A on the financial performance of banks in Pakistan. His study concentrated on the performance of three commercial banks that had merged between 2000 and 2012. The analysis was done using ratios which were based on the secondary data acquired from the annual reports of the banks. He used paired t-test to compare the date before and after the mergers. The study revealed that some banks showed improved performance while others did not as evidenced by the profitability ratios. The study also revealed that financial performance of banks deteriorated in the initial years after the mergers and/or acquisitions but thereafter there was a slight increase in the financial performance of the banks.

2.4.2 Local Studies

Mureithi (2013) explored the effect of M&A on financial performance of Kenyan commercial bank. The research used causal research design. Sixteen (16) commercial banks engaged in M&A between 2000 and 2012 constituted the unit of analysis for the study. ROE and return on equity used as indicators of financial performance. Study found positive relationship and profitability generally increased following post-merger activity. This study did not focus on Operating performance using accounting measures but it was based on event studies.

Mboroto (2013) studied the influence of M & A on Kenyan petroleum firm's financial performance with focus on the petroleum industry in Kenya by looking at the firms that merged

during the period 2000 to 2012. He analyzed the NSE annual statements and financial reports and made comparisons between the mean of the ratios for the 3 year period before the merger and 3 year period after the merger. He found that M&A did not significantly affect the financial performance of petroleum firms in Kenya; specifically on the liquidity and solvency ratio while on the other hand; M&A's had a significant impact on profitability as reflected by the ROA.

Kivindu (2013) explored the influence of M&A on Kenyan bank's profitability through undertaking a comparison of a pre-merger and post-merger profitability among 24 Kenyan banks that had underwent M&A. ROE, ROA, capital adequacy ratio, profit before tax was analyzed in the study. The findings indicated that more consolidations were undertaken by institutions with weak capital so as to attain synergies and accrue economies of scale leading to increased profitability rather than aspiring to be quoted in stock exchanges and paying unnecessary costs. Furthermore, post merger firms benefited from M & A due to improved capital base, competitiveness and efficiency.

Mitema (2014) studied the effect of M&A on the value creation focusing on the insurance companies in Kenya. The research used a sample of 4 insurance companies in Kenya that had gone through a merger or acquisition over the period of 2000 to 2014. The study findings showed a positive significance relationship an indication that M&A create value and also have positive impact on both book and fundamental value of the listed firms who engaged in M&A. Descriptive research design and regression analysis was used. This study looked at firms in most industry sector listed and it used event study methodology to see if M&A have an impact on the shareholders returns.

Barasa (2015) examined the impact of M & A on share prices of companies quoted at the NSE using CAPM event study. He used a sample of nine firms that had merged during a period of 2007 - 2014. The study found that the merger and acquisition announcements had strong impacts on total accumulated share returns for the various quoted firms before and after the announcements. He therefore, concluded that M&A are indeed positively influenced returns for shareholders in short term.

Mwanza (2016) conducted a study on the effect of M & A on financial performance of Kenyan insurance companies. The population was the M&A that took place between years 2010 and 2013 thus a census approach was adopted. Two year pre-merger and post-merger data was collected from secondary sources and compared to determine whether there was significant change in performance after the merger. The study employed various measures of financial

performance which included ROE, return on capital employed, net income margin, net working capital and leverage. The study established that after the merger, ROE and return on capital employed significantly improved and concluded that M&A improve the financial performance of Kenyan insurance firms. The key limitation of the study was that the two-year duration for which was analyzed in too short to conclusively determine the impact of M & A on the financial performance of the merging firms.

Kiprotich (2017) studied on the influence of M & A on value of insurance firms listed at the NSE. The study's population was made up the 12 insurance companies that had merged and/or had been acquired over the duration of 17 years between 2000 and 2016.. Regression results before and after merge and acquisition was presented. Before merger, profitability, firm size, liquidity, leverage had a positive and significant relationship with firm value. After post-merger and acquisition regression results showed that profitability, firm size, liquidity, leverage remained significantly and positively related with firm value.

2.5 Conceptual Framework
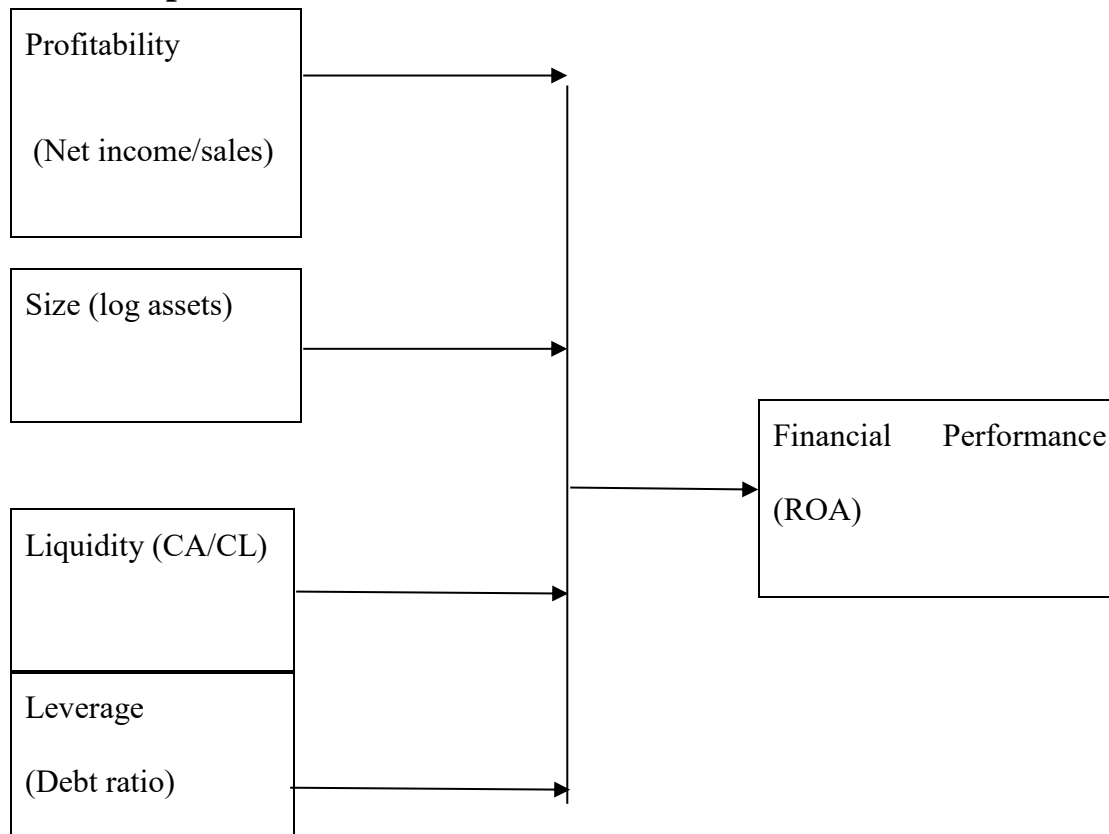
Independent variables   **Dependent   variable**

Source: Author (2018)

Figure 2.1: The Conceptual Model

Independent variables include profitability as measured by net income over sales, Liquidity given as current assets/ current liabilities, firm size given by natural logarithm of total assets and leverage as measured by debt ratio given as long-term debt/ (shareholders equity + long term debt). Financial performance was the explainable variable and it was determined by ROA.

2.6 Summary of the Literature Review

This section looks into the theories postulated for M & A like the efficiency theory, agency theory and the hubris theory. The section further outlines the financial performance determinants such as; M & A, management efficiency, firm size, the age of the company, capital structure and macro-economic factors. Various empirical studies on the subject of M & A both on the global and local perspective are also reviewed in the section.

The section further reveals evidence of other research on M & A that have failed to address the impact of M & A on Kenyan insurance companies' financial performance. Additionally, the outcomes seem to change from one firm to the other. Moreover, findings from the research depict inconsistencies and incompatibilities based on analytical model applied and the markets. Local studies carried are not decisive in their results and it's this gap the current study filled.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

In order to determine the influence of M & A on financial performance of Kenya insurance companies, a research methodology is necessary to outline how the research was carried out. This chapter has four sections namely; research design, data collection, diagnostic tests and data analysis.

3.2 Research Design

A descriptive cross-sectional research design was employed in this research in investigating the connection between M & A and financial performance of Kenya insurance companies. Descriptive design was utilized as the researcher is interested in finding out the state of affairs as they exist (Khan, 2008). This research design is appropriate for the study as the researcher is familiar with the phenomenon under investigation but want to know more in terms of the nature of relationships between the study variables. In addition, a descriptive research aims at providing a valid and accurate representation of the study variables and this helps in responding to the research question (Cooper & Schindler, 2008).

3.3 Target population

A study population relates to a large set of objects or people that is the core focus of the researcher (Burns & Burns, 2008). The population of the study is made up of all the 9 insurance companies that had merged and/or had been acquired over the duration of 15 years between 2000 and 2015.

3.4 Data Collection

The research used secondary data from financial statements of the merged firms before and after the merger. Secondary data was obtained from insurance company statutory filings with the IRA, IRA annual and semi-annual publications and published insurance companies' financial statements. From these sources, panel data (time series and cross sectional data) was collected. The end result was information detailing the independent variables and dependent variable for the insurance firms that have undergone M & A between 2000 and 2018.

3.5 Data Analysis

SPSS version 21 was applied in analyzing the data. Pre and post-merger performance ratios was computed for the entire set of sample firms which had gone through M&A during the selected period and their means, variances and standard deviations used for descriptive statistics. The pre and post M&A performance ratios was compared to see if there is any statistically significant change in performance of the companies after M&A firms using paired sample t-test. Also Pearson Correlation coefficient test and regression was employed to assess the significance level.

3.5.1 Analytical Model

This study was use a sampled t-test to determine the extent to which total variation in the dependent variable (financial performance) is influenced by the variation in the independent variables. This used to test significance of the independent variables in determining the variations in the dependent variable in both the pre-merger and post-merger periods.

The following regression model was used:

$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon.$

In which: Y = Financial performance as measured by ROA

α = y intercept of the regression equation.

$\beta_1, \beta_2, \beta_3, \beta_4,$ = are the regression slope

X_1 = Profitability, as given by, net income over sales

X_2 = Liquidity, as given by current assets divided by current liabilities

X_3 = Size, as given by; natural logarithm of total assets

X_4 = Debt ratio given as long term debt / (shareholders equity + long term debt)

ε = error term

3.5.2 Tests of Significance

Significance level is the possibility that a random sample does not represent the entire population and it is used to measure the margin of error. A lower significant level implies higher levels of confident that the results was replicated on the entire population. Higher significance levels implies higher margin of error and hence lower confidence levels. The study used a two tailed pair t-test at 5% significance level to test the differences of the means of the ratios before and after the merger.

CHAPTER FOUR

PRESENTATION AND DISCUSSION OF RESULTS

4.1 Introduction

This section majors on the analysis of the secondary data collected from the various sources including company financial reports and insurance regulatory authority annual reports in establishing the influence of M&A on the financial performance of insurance companies Using descriptive statistics, correlation analysis and regression analysis, the results were presented in table forms as shown in the following sections. The study applied Pearson Correlation coefficient test and multiple linear regressions to determine the extent to which total variation in the dependent variable (financial performance) is influenced by the variation in the independent variables before and after mergers.

4.2 Descriptive Statistics

This section presents the descriptive results of the study during pre and post-merger, measures of central tendency, the trends analysis including insurance companies average ROA, profitability ratio, liquidity, firm size measures as log of total assets and average leverage ratio.
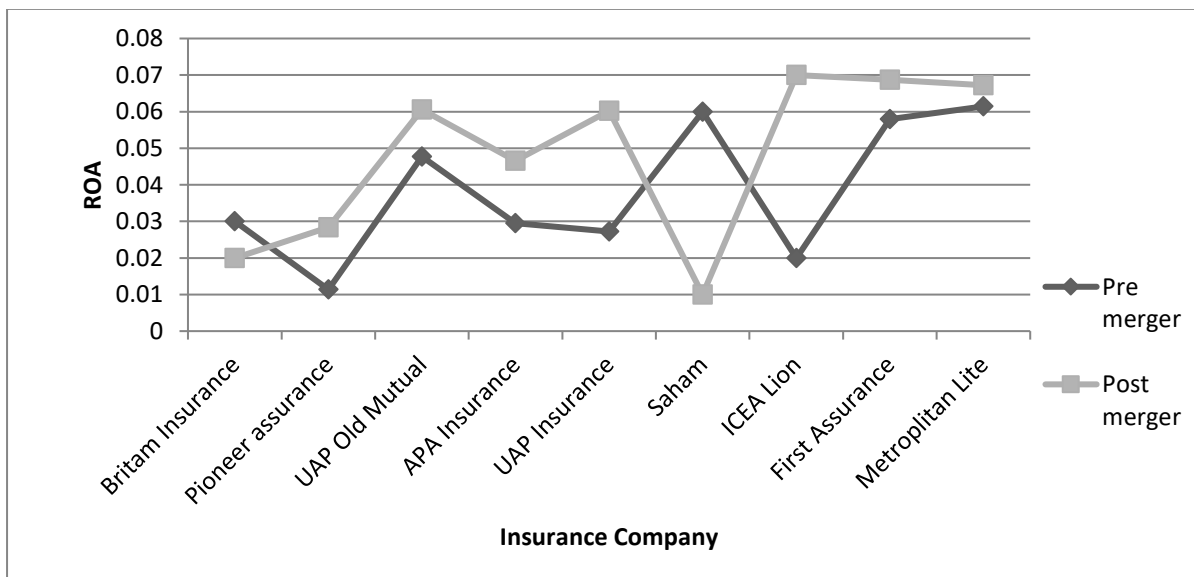
Figure 4.1: Comparison of ROA pre-merger and post-merger

From the analysis of the companies' ROE before and after merger, it was found that all the M & A resulted in an increase in ROA except for Britam Insurance and Saham. ICEA Lion Limited recorded the highest increase in ROA of 0.07284 after the merger. Britam Insurance and Saham recorded the lowest ROE. It is clear from the results in figure 4.1 that merger and acquisition leads to the rise of ROA.
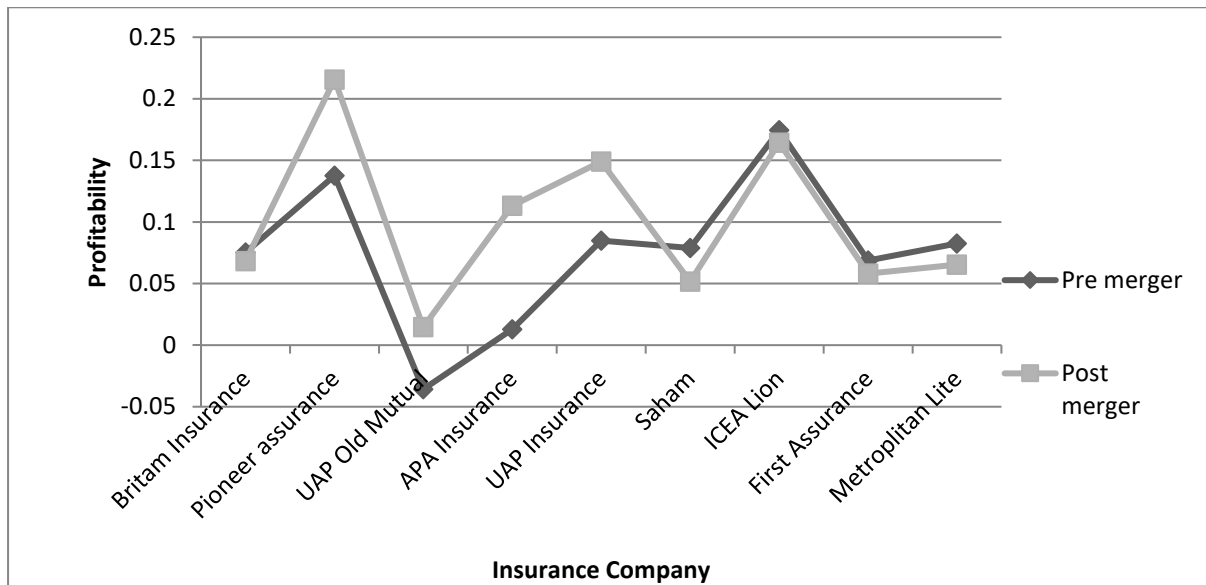
Figure 4.2: Comparison of Profitability ratio pre-merger and post-merger

Figure 4.2 shows profitability ratio of insurance companies before merge and post merge. From the analysis of the companies' profitability ratios before and after the merger and acquisition, it was found that Pioneer Insurance, APA Insurance and UAP Insurance recorded the significant improvement in the profitability after merge and acquisition. Further, results shows that Metropolital Lite recorded a fairly high profitability ratio after merger while and UAP Old Mutual recorded a slightly small increase after merger. The profitability ratio for Saham dropped drastically after merger.
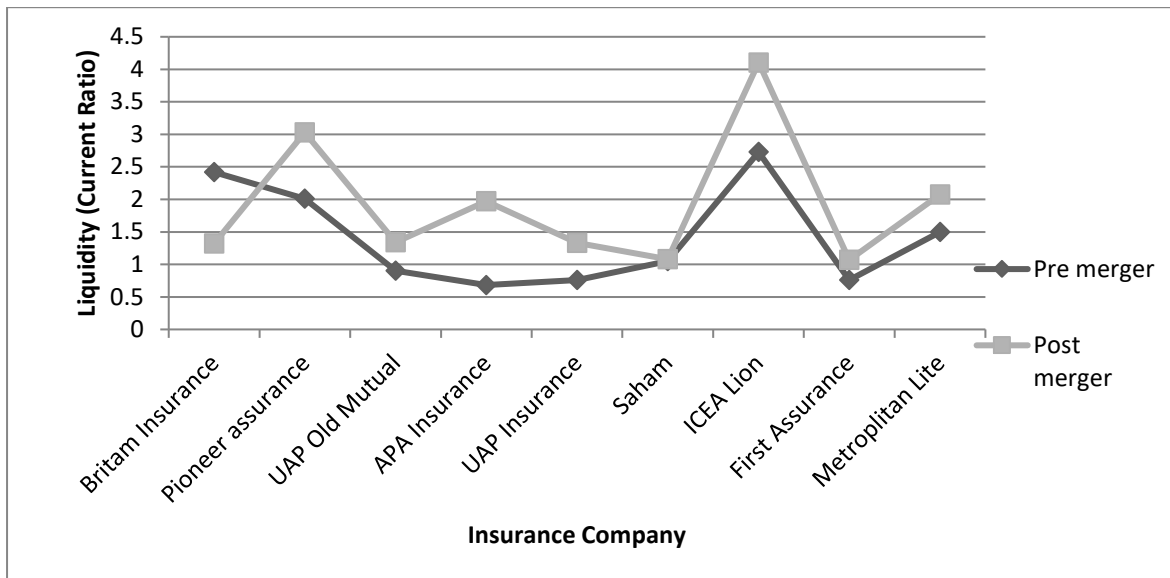
Figure 4.3: Comparison of Liquidity pre-merger and post-merger

Figure 4.3 shows liquidity of insurance firms before and after merger. The analysis of the companies' liquidity before and after merger showed that the average liquidity ratio for all the insurance companies except for Britam Insurance increased after merger. ICEA Lion posted the highest increase in liquidity after merger. This was followed closely by APA Insurance and Pioneer Insurance respectively. The results imply that merger and acquisition boosts the liquidity state of insurance firms.
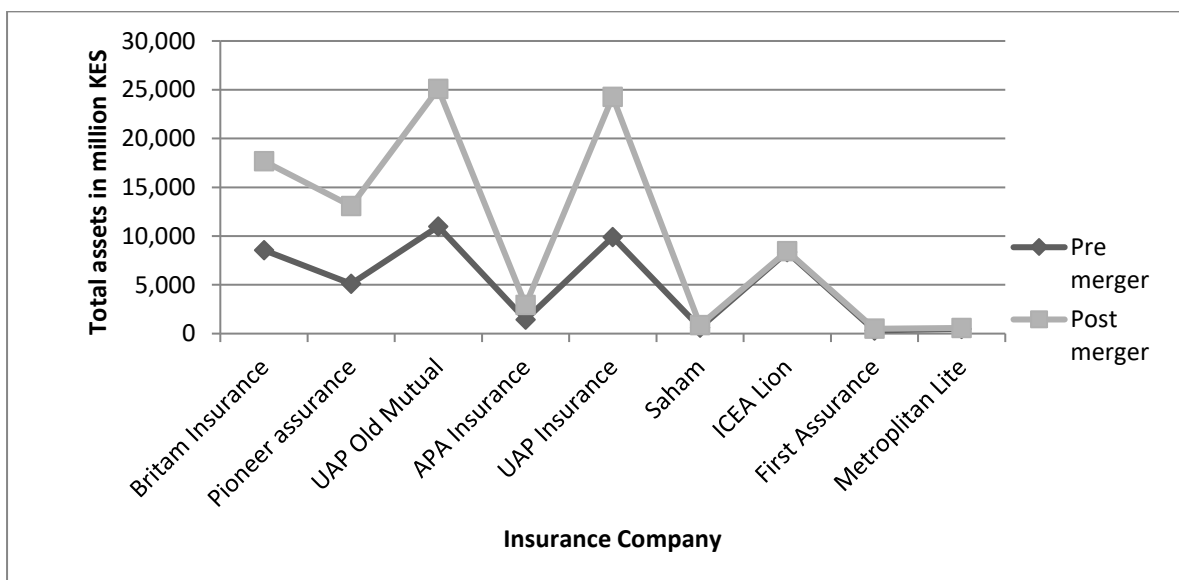
Figure 4.4: Firm size pre-merger and post-merger

Figure 4.4 illustrates insurance firm size measured in total assets before and after merger. The analysis of the companies' total assets before and after merger showed that the average total assets increased for all the insurance firms post-merger. Results showed that UAP Insurance and UAP Old Mutual realized the highest increase in total assets after merger. This was followed closely by Britam Insurance. The results imply that firm size measured in total assets increases after merger.
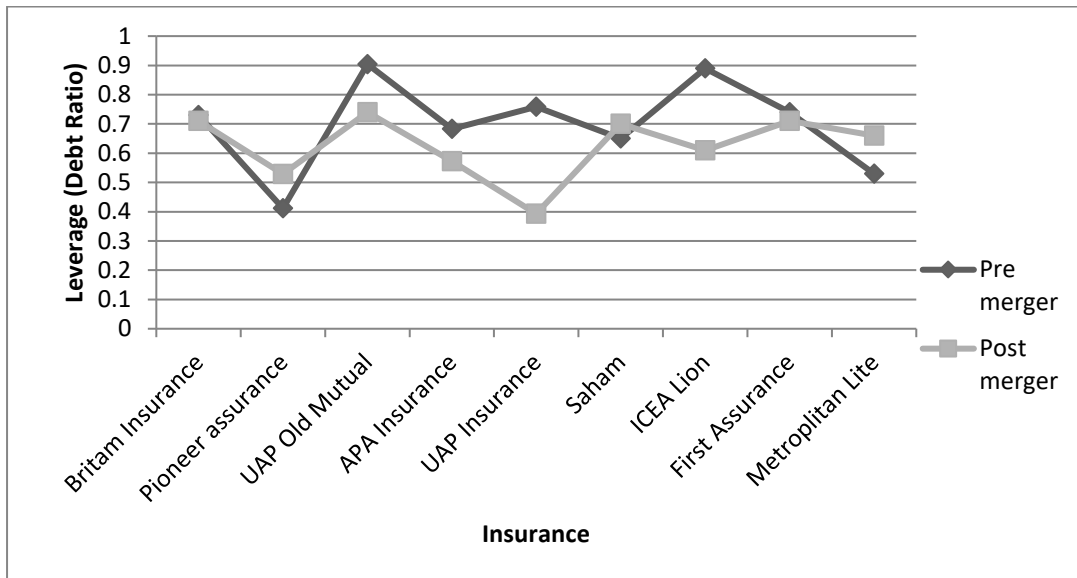
Figure 4.5: Firm's Leverage pre-merger and post-merger

Figure 4.5 shows insurance firm leverage measured as debt ratio before and after merger. The analysis of the companies' leverage revealed that the post-merger leverage was lowest in UAP Insurance followed by Pioneer Insurance. Results further showed that UAP Old Mutual, Saham and First assurance operated at highest leverage after merger. Less leveraged company attracts more investors than a more leveraged company.

4.3 Sampled T-statistics

The results of the paired sampled t-statistics were as tabulated in the ensuing table.

Table 1.1: Sampled T-statistics before and after Merger

	Mean		Std. Deviation		T-statistics		Std. Error Mean		Sig. (2-tailed)
	Pre-merge r	Post-merger	Pre-merger	Post-merger	Pre-merger	Post-merger	Pre-merger	Post-merger	
ROA	0.03880	0.04854	0.01940	0.02353	5.9420	3.907	0.00647	0.00784	.041
Profitability	0.10002	0.07547	0.06490	0.06141	3.0630	4.030	0.02163	0.02047	.036
Liquidity	1.42321	1.92383	0.78120	1.03105	7.7110	6.879	0.26040	0.34368	.020
Total assets (million KES)	5083.9	10388.3	4442.6	10083.0	6.8901	5.017	1480.9	3361.0	.032
Leverage	0.69959	0.62489	0.15758	0.11216	7.6490	6.372	0.05253	0.03739	.027

From the analysis the findings clearly show that before the merger average ROE mean difference was 0.03880 with a standard deviation of 0.01940 and mean difference of 0.04854 and standard deviation of 0.02353 after the merger. The p value is .041<0.05 and therefore we conclude that there is statistically significant change in ROA before and after mergers. The results agree with Fatima and Shehzad (2014) who looked into the impact of M&A on Pakistan insurance companies' financial performance by analyzing six financial ratios and concluded that mergers' objectives were not clearly obtained, economies of scale were not achieved neither was synergy created.

Profitability had a mean difference of 0.10002 and standard deviation of 0.06490 and mean difference of 0.07547 and standard deviation of 0.06141 after the merger. The p value is .036 <0.05 and therefore we conclude that there is statistically significant change in profitability before and after mergers. The findings agree with Olalekan (2012) who studied the implication of M&A's on the profitability and other performance measures on commercial banks in Nigeria and found that there was a notable connection between the capital base of the commercial banks and their profitability before the merger and after the merger.

Liquidity had a mean difference of 1.42321 and standard deviation of 0.78120 and mean difference of 1.92383 and standard deviation of 1.03105 after the merger. The p value is .020<0.05 and therefore we conclude that there is statistically significant change in liquidity before and after mergers. Firm size measured as total assets had a mean difference of KES 5083.9 million and standard deviation of KES 4442.6 million and mean difference of KES 10388.3 million and standard deviation of KES 10083.0 million after the merger. The p value is .032<0.05 and therefore we conclude that statistically significant change exists in total assets before and after mergers.

Debt ratio measured as leverage had a mean difference of 0.69959 and standard deviation of 0.15758 and mean difference of 0.62489 and standard deviation of 0.11216 after the merger. The p value is .027<0.05 and therefore we conclude that there is statistically significant change in leverage before and after mergers.

4.4 Correlation Analysis

Pearson correlation was employed to determine the association of variables before merger, after merger and acquisition of insurance companies. Results of correlation before merger are shown in table 4.1.

Table 4.1: Correlation analysis Pre merger

		ROA	Profitability	Liquidity	Firm size	Leverage
ROA	Pearson Correlation	1.000				
	Sig. (2-tailed)					
Profitability	Pearson Correlation	.525	1.000			
	Sig. (2-tailed)	.006				
Liquidity	Pearson Correlation	.479	.409	1.000		
	Sig. (2-tailed)	.042	.274			
Firm size	Pearson Correlation	.537	.157	.311	1.000	
	Sig. (2-tailed)	.036	.686	.415		
Leverage	Pearson Correlation	-.223	-.371	-.045	.55	1.000
	Sig. (2-tailed)	.043	.327	.908	.125	

From the analysis of the correlation analysis before the M & A, it was found that there exists a positive correlation between profitability and financial performance of insurance companies

(r= .525, p = .006). The results agree with Masud (2015) who studied the influence of M & A on the financial performance of banks in Pakistan and found that some banks showed improved performance while others did not as evidenced by the profitability ratios.

The results also revealed that there is positive correlation between liquidity and financial performance of insurance companies (r= .479, p=.042). Further, correlation results indicated that there exist a positive relationship between firm size measured as logarithm of total assets and financial performance of insurance companies (p= .537, p=.036). Finally, correlation results showed that there is a negative relationship between leverage and financial performance of insurance companies (p= -.223, p=.043). Table 4.2 shows results of correlation after merger.

Table 4.2: Correlation analysis Post-merger

		ROA	Profitability	Liquidity	Firm size	Leverage
ROA	Pearson Correlation	1.000				
	Sig. (2-tailed)					
Profitability	Pearson Correlation	.628	1.000			
	Sig. (2-tailed)	.022				
Liquidity	Pearson Correlation	.524	.681	1.000		
	Sig. (2-tailed)	.037	.043			
Firm size	Pearson Correlation	.549	.222	.094	1.000	
	Sig. (2-tailed)	.034	.566	.810		
Leverage	Pearson Correlation	-.112	-.350	-.274	-.293	1.000
	Sig. (2-tailed)	.045	.356	.476	.443	

From the analysis of correlation analysis after the merger, the findings shows that there is a positive correlation between profitability and financial performance of insurance companies (r= .628, p = .022). The coefficient changes to a higher value an indication of stronger association after merger. Results of the correlation also revealed that there is a strong positive correlation between liquidity and financial performance of insurance companies (r= .524, p=0.037). The coefficient increased slightly after merge as compared to the coefficient before merge. Further, correlation outcomes showed that there is a strong positive connection between firm size measured as logarithm of total assets and financial performance of insurance companies (p= .549, p=.034). The coefficient of association increased slightly after merge and acquisition. The correlation association for leverage showed that there is a negative relationship between leverage and financial performance of insurance companies (p= -.112, p=.045). The coefficient of association reduced after merge and acquisition indicating a negative association

between leverage and financial performance of insurance companies after merge and acquisition.

4.5 Regression analysis

Table 4.3 shows R^2 results. Financial performance was regressed against, profitability, firm size, liquidity and leverage. The regression analysis was conducted at 5% significance level. The study obtained the model summary statistics as displayed in table 4.3.

Table 4.3: Model summary pre-merger and post-merger

Model	R	R^2	Adjusted R^2	Std. Error of the Estimate
Pre-merger	.724	.655	.509	.01046081531
Post-merger	.885	.748	.704	.03070985908

Source: Research Findings (2018)

From the outcome in table 4.3, the value of R^2 was before merger was .655, indicating that 65.5 percent of the deviations in financial performance of insurance companies are explained by changes in profitability, firm size, liquidity and leverage. The R square results after merge was 74.8%. The results of the model summary before and after merge and acquisition differed significantly. There was a significant change in R square before and after merge in indication of improved explanatory power of the predictor variables. Figure 4.4 reveals the ANOVA outcomes of the study.

Table 4.4: ANOVA

Model		Sum R^2	df	Mean Square	F	Sig.
Pre-merger	Regression	4.003	6	.001	15.878	.0327
	Residual	1.000	129	.000		
	Total	**5.003**	**135**			
Post-merger	Regression	6.001	5	.000	17.174	.0231
	Residual	2.004	130	.001		
	Total	**8.005**	**135**			

30

The significance value is 0.000 which is less than p=0.05. The Anova results before and after merge were statistically significant. This implies that the model was statistically significant in behavior of profitability, firm size, liquidity and leverage before and after merge. The F value derived indicates that the data used was linear and therefore can be used for regression analysis. The regression results of the model before merge and acquisition is shown in table 4.5.

Table 4.5: Model Coefficients before merge and acquisition

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.077	.026		3.025	.043
Profitability	.130	.022	.769	5.909	.034
Liquidity	.203	.062	.460	3.274	.039
Firm size	.215	.039	.365	5.537	.027
Leverage	-.231	.065	-.208	-3.554	.034

Using a significance level of 5%, any independent variable having a significance value greater than 5% is considered not statistically significant. It was revealed that firm size measured as log of assets, profitability and leverage were statistically significant in explaining financial performance of insurance companies at 5% level of significance.

From the above results, it is clear that profitability has a positive and statistically significant relationship with financial performance of insurance companies (r = .130, p = .034), liquidity has a positive and statistically significant relationship with financial performance of insurance companies (r = .203, p = .039) while firm size has a positive and statistically significant relationship with financial performance of insurance companies (r =.215, p = .027). Finally, regression results showed that leverage has a negative and statistically significant relationship with financial performance of insurance companies (r = -.231, p = .034).

The regression equation before merge and acquisition was:

$Y = .077 + .130X_1 + .203X_2 + .215X_3 - .231X_4$

Where,

Y = Financial performance

X_1 = Profitability

X_2 = Liquidity

X_3 = Firm size

X_4 = Leverage

On the estimated regression model above, the constant = .077 means that if selected dependent variables (profitability, firm size, liquidity and leverage) are put at zero, financial performance measured as ROA will be .077. A unit rise in profitability would cause a rise in performance of an insurance company by .130 units. A unit rise in liquidity would cause a rise in financial performance of an insurance company by .203 units. Further, a unit increase in firm size measured as log of total assets would lead to an increase in performance of an insurance company by .215 units. Finally, a unit rise in leverage would cause a drop in performance of an insurance company by -.231 units. The regression results of the model post merge and acquisition is shown in table 4.6.

Table 4.6: Model Coefficients post merge and acquisition

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	.064	.087		0.739	.501
Profitability	.169	.062	.440	2.726	.045
Liquidity	.211	.014	.484	15.071	.026
Firm size	.255	.029	.109	8.793	.034
Leverage	-.135	.043	-.165	-3.139	.041

Regression results post merge and acquisition shows that profitability has a positive and statistically significant relationship with financial performance of insurance companies (r = .169, p = .045). For profitability there was an increase in the coefficient from .130 to .169 after merge and acquisition. The results of liquidity had a positive and statistically significant relationship with firm value (r = .211, p = .026). Coefficient improved from .203 to .211 after

merge and acquisition. Firm size had a positive and statistically significant relationship with financial performance of insurance companies (r =.255, p = .034). For firm size the regression coefficient improved slightly from .215 to .255 after merge and acquisition. Further, regression results showed that leverage has a negative and statistically significant relationship with firm value (r = -.135, p = .041). The coefficient improved from-.231 to -.135 post merger.

The regression equation post merge and acquisition was:

$Y = .064 + .169X_1 + .211X_2 + .255X_3 - .135X_4$

Where,

Y = Firm value

X_1 = Profitability

X_2 = Liquidity

X_3 = Firm size

X_4 = Leverage

On the estimated regression model above, the constant = .064 means that if selected dependent variables (profitability, firm size, liquidity and leverage) are put at zero, financial performance of insurance company measured as ROA will be .064. A unit rise in profitability would cause a rise in financial performance of insurance company by .169 units. A unit rise in liquidity would cause a rise in financial performance of insurance company by .211 units. Further, a unit increase in firm size measured as log of total assets would lead to an increase in financial performance of insurance company by .255 units. Finally, a unit rise in leverage would cause a drop in firm value by -.135 units.

4.6 Discussion of Research Findings

Model results indicated that for profitability there was an increase in the coefficient from .130 to .169 after merge and acquisition. The change in the coefficient implies that after merger, the effect of profitability on financial performance of insurance firms improved. The results agree with Kainika (2016) who examined the effects of M & A on organizational performance of Kenyan Insurance Industry and established that the effect of profitability on financial performance of insurance company increased after merger.

It was also established that for liquidity there was an increase in the effect of coefficient from .203 to .211 after merge and acquisition. The change in the coefficient implies that after merger, the effect of liquidity on financial performance of insurance companies improved. The results agree with Almajali *et al.,* (2012) noted that firm's liquidity may have impact on insurance companies' financial performance.

The study established that regression coefficient of firm size there was from .215 to .255 after merge and acquisition. The change in the coefficient implies that after merger, the effect of firm size on financial performance of insurance companies improved. Company size as well influences the financial performance of the firm. Size can influence firm performance positively, since larger firms can leverage on their size to obtain better deals in financial as well as product or other factor markets. The results agree with Shim (2007) that the influence of firm size on financial performance of insurance companies improves significantly after merger and acquisition.

For leverage, regression coefficient of firm size there was from -.231 to -.135 after merge and acquisition. The change in the coefficient implies that after merger, the insurance companies became less leveraged. The outcomes are in line with the research by Ambrosini, (2003) who discovered a great positive correlation between leverage and ROE adding that leverage can provide opportunities for achieving substantial savings, significant improvements in performance.

Model summary results indicated that value of R square was before merger was .655, indicating that 65.5 percent of the deviations in financial performance of insurance companies are explained by changes in profitability, firm size, liquidity and leverage. The R square results after merge was 74.8%. The results of the model summary before and after merge and acquisition differed significantly. There was a significant change in R square before and after merge in indication of improved explanatory power of the predictor variables.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

The chapter shows the summary of research findings from the study on how M & A influence value of Kenya insurance companies. Further, it highlights policy recommendations in regard to M & A in insurance. The various study limitations are highlighted in this chapter as well and further areas for research.

5.2 Summary of the findings

The researcher was seeking to investigate the influence of M & A on financial performance of Kenyan insurance companies. The study population was made up of all the 12 insurance companies that had merged and/or had been acquired over the duration of 17 years between 2000 and 2016. The pre and post M&A performance ratios was compared to see if there is any statistically significant change in value of the companies after M&A firms using paired sample t-test. Also Pearson Correlation coefficient test and regression was applied in assessing the significance level.

From the analysis of the companies' financial performance before and after merger, it was found that all the M & A resulted in an increase in financial performance after the merger. From the analysis of the companies' profitability ratios before and after the merger and acquisition, it was found that Pioneer Insurance, APA Insurance and UAP Insurance recorded the significant improvement in the profitability after merge and acquisition. Further, results shows that Metropolital Lite recorded a fairly high profitability ratio after merger while and UAP Old Mutual recorded a slightly small increase after merger. The profitability ratio for Saham dropped drastically after merger.

The analysis of the companies' liquidity before and after merger showed that the average liquidity ratio for all the insurance firms increased after merger. The analysis of the companies' liquidity before and after merger showed that the average liquidity ratio for all the insurance companies except for Britam Insurance increased after merger. ICEA Lion posted the highest increase in liquidity after merger. This was followed closely by APA Insurance and Pioneer Insurance respectively. The results imply that merger and acquisition boosts the liquidity state

of insurance firms. Less leveraged company attracts more investors than a more leveraged company.

The analysis of the companies' total assets before and after merger showed that the average total assets increased for all the insurance firms post-merger. Results showed that UAP Insurance and UAP Old Mutual realized the highest increase in total assets after merger. This was followed closely by Britam Insurance. The results imply that firm size measured in total assets increases after merger.

Further, the analysis of the companies' leverage revealed that the post-merger leverage was lowest in UAP Insurance followed by Pioneer Insurance. Results further showed that UAP Old Mutual, Saham and First assurance operated at highest leverage after merger. Less leveraged company attracts more investors than a more leveraged company.

Regression results before and after merge and acquisition was presented. Before merge, profitability, firm size, liquidity, leverage had a positive and significant relationship with financial performance of insurance companies. After post merge and acquisition regression results showed that profitability, firm size, liquidity, leverage the beta coefficients improved significantly

Model summary results indicated that value of R square was before merger was .655, indicating that 65.5 percent of the deviations in financial performance of insurance companies are explained by changes in profitability, firm size, liquidity and leverage. The R square results after merge was 74.8%. The results of the model summary before and after merge and acquisition differed significantly. There was a significant change in R square before and after merge in indication of improved explanatory power of the predictor variables.

5.3 Conclusions

The study found that profitability had a positive and statistically significant relationship with financial performance of insurance companies before and after merge. The study therefore concludes that an increase in in profitability would lead to an increase in financial performance of insurance companies. M & A in the insurance industry is one of the ways to boost revenue growth, build economies of scale and ultimately raise profitability.

The study found that liquidity has a positive and statistically significant relationship with financial performance of insurance companies and therefore it is concluded that in an increase

in liquidity leads to an increase in financial performance of insurance companies. When firms merge, their liquidity strength improves.

Firm size was found to have a positive and statistically significant relationship with financial performance of insurance companies and this means that a rise in the unit in firm size causes a rise in financial performance of insurance companies. Merging and acquisition may lead to improved asset base of the companies. As a result, their coming together improves economies of scale expanding growth.

It was also concluded that leverage has a negative and statistically significant relationship with financial performance of insurance companies. A unit rise in leverage causes a drop in financial performance of insurance companies. Leverage involves financing company operation through debt. As a result of merge and acquisition, the new company is able to finance their operations without borrowing.

5.4 Recommendations for policy

From the study, insurance firms can improve their profitability by merging. By doing so the firms can identify synergies arising from economies of scale, increasing efficiency and diversifying risks. 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. Acquisitions also enhance increased revenue by absorbing a major competitor and thereby increasing market share and enhancing market dominance and reaching economies of scale. In case a firm can't improve inwardly for lack of physical or managerial resources, it can improve or grow outwardly by uniting its activities with other firms via M & A which may aid in accelerating the speed of a firm's growth in a convenient and cheaper way.

The analysis of the companies' total assets before and after merger showed that the average total assets increased for all the insurance firms post-merger. The advocates for merge and acquisition in case of resource strain. Through merge and acquisition, insurance firms can increase their asset base which will boost their competiveness in the market place. They are also able to minimize liabilities by reducing the debt equity ratio. Large organizations are able to access financial resources at a lower cost as well. Asset growth also results from acquisition. This is the increase in a firm's assets that can be achieved by merger and acquisition, after

merger the acquiring firm takes control of the target asset and so manages its assets and those of the target, this leads to an increase in its assets after the merger.

A recommendation is given that merged insurance firms ought to maintain leverage ratio at a standard level because that too much debt can be unsafe for a merged insurance and its investors as uncontrolled debt levels can cause credit downgrades whereas at the same time low debt-to-equity ratios may also reveal that a company is not misusing the increased gains that financial leverage may bring. A recommendation is given that proactive fiscal policy and prudent monetary policy be enacted to minimize firms' leverage by such measures as promoting M & A, revitalizing stock assets, optimizing debt structure, carrying out debt-for-equity swap programs and developing equity financing.

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.

5.5 Suggestions for further research

Future studies should explore further reasons for M & A apart from firm value. The factors may include competition and pricing strategies. The dependent variable can also be measured using ROE for comparison purpose with ROA.

5.6 Limitations of the study

There are other factors that influencing financial performance like management efficiency. This study considered M & A as the only driver of financial performance therefore the study results may not be conclusive. Further study may include the variable.

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APPENDICES

Appendix I: Data Collection Sheets

Insurance/Average	ROA		profitability		liquidity		Firm size in million KES		leverage	
	pre	post	pre	post	pre	post	pre	post	pre	post
Britam Insurance	0.030223	0.020765	0.068333	0.0753	2.4185	1.319375	8,557	17,674	0.730877	0.71054
Pioneer assurance	0.011357	0.028407	0.2157	0.137733	2.011357	3.028407	5098	13074	0.411357	0.528407
UAP Old Mutual	0.04772	0.060567	0.014625	-0.0358	0.904079	1.339933	10978	25097	0.904079	0.739933
APA Insurance	0.029497	0.046533	0.113113	0.01275	0.682731	1.972733	1437	2953	0.682731	0.572733
UAP Insurance	0.027233	0.06025	0.148933	0.084875	0.758133	1.3296	9911	24288	0.758133	0.392906
Saham	0.067489	0.010354	0.051646	0.078804	1.051646	1.078804	605	871	0.650877	0.70742e
ICEA Lion	0.020234	0.070344	0.16443	0.174402	2.726825	4.104475	8353	8453	0.890533	0.610364
First Assurance	0.057982	0.068724	0.057982	0.068724	0.757982	1.068724	329	498	0.749435	0.710963
Metroplitan Lite	0.065434	0.072434	0.065434	0.082434	1.4976	2.072434	487	587	0.530755	0.66497

Appendix I: List of Insurance M & A between 2000 and 2015

Name	Merged with	Current name	Year of M&A
Pioneer Assurance	Fidelity Assurance	Pioneer Assurance	2002
Pan Africa Insurance	Apollo	APA Insurance	2004
ICEA Insurance	LION Assurance	ICEA LION	2012
Saham Group	Mercantile insurance	Saham	2013
Britam Insurance	Real Insurance	Britam General	2013
UAP (K) Ltd	Century insurance	UAP	2013
UAP Ltd	Old mutual ltd	UAP old mutual	2014
Metropolitan life insurance	Canon life Assurance	Metropolitan life insurance	2015
First Assurance	Barclays Africa	First Assurance	2015