EFFECT OF MERGERS AND ACQUISITIONS ON FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

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DECLARATION

I declare that this research project is my original work and has not been submitted for a degree in any other university for purposes of examination.

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

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TABLE OF CONTENTS

DECLARATION .... **ii**

LIST OF TABLES .... **vii**

LIST OF FIGURES .... **viii**

LIST OF ABBREVIATIONS .... **ix**

CHAPTER ONE **1**

INTRODUCTION **1**

1.1 Background of the Study 1

1.1.1 Mergers and Acquisitions 2

1.1.2 Financial Performance 4

1.1.3 Mergers and Acquisitions and Financial Performance 5

1.1.4 Commercial Banks in Kenya 7

1.2 Research Problem 7

1.3 Research Objective 10

1.4 Value of the Study 10

CHAPTER TWO **12**

LITERATURE REVIEW **12**

2.1 Introduction 12

2.2 Theoretical Review 12

2.2.1 Efficiency Theory 12

2.2.2 Agency Theory 13

2.2.3 Hubris Theory 15

2.2.4 Monopoly Theory 16

2.3 Determinants of Financial Performance 18

2.3.1 Leverage 18

2.3.1 Liquidity 18

2.3.3 Management Efficiency..19

2.3.4 Firm Size...20

2.4 Empirical Review...20

2.4.1 Global Studies..20

2.4.2 Local Studies 22

2.5 Conceptual Framework..24

2.6 Summary of Literature Review..25

CHAPTER THREE 27

RESEARCH METHODOLOGY 27

3.1 Introduction...27

3.2 Research Design...27

3.3 Study Population...27

3.4 Data Collection 28

3.5 Data Analysis...28

3.5.1 Diagnostic Tests 28

3.5.2 Analytical Model 29

3.5.3 Tests of Significance 29

CHAPTER FOUR **30**

DATA ANALYSIS AND FINDINGS **30**

4.1 Introduction 30

4.2 Descriptive Statistics 30

4.2.1 ROA 30

4.2.2 Leverage 31

4.2.3 Liquidity 33

4.2.4 Management Efficiency 34

4.2.5 Firm Size 36

4.4 Diagnostic Tests 37

4.4.1 Normality Tests 37

4.4.2 Homoscedasticity Test 38

4.4.3 Multicollinearity Test 39

4.4.3 Test of Stationarity 40

4.4 Paired Samples Test 40

4.5 Correlation Analysis 43

4.6 Discussion of Research Findings 44

CHAPTER FIVE **47**

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS **47**

5.1 Introduction 47

5.2 Summary 47

5.3 Conclusions 48

5.4 Recommendations for policy 49

5.5 Limitations of the Study...50

5.6 Recommendations for Further Studies..51

REFERENCES...52

APPENDICES 56

APPENDIX 1: LIST OF COMMERCIAL BANKS MERGED OR ACQUIRED BETWEEN 2008 AND 2018...56

LIST OF TABLES

Table 4.1: Descriptive Statistics of ROA 30

Table 4.2: Descriptive Statistics of Leverage 31

Table 4.3: Liquidity Descriptive Statistics 33

Table 4.4: Management Efficiency 34

Table 4.5: Firm Size Descriptive Statistics 36

Table 4.6: Shapiro-Wilk Test of Normality 37

Table 4.7: Test for Heteroscedasticity 38

Table 4.8: Multicollinearity Test 39

Table 4.9: Serial Correlation 40

Table 4.10: Paired Samples Test 41

Table 4.11: Correlation Matrix 43

LIST OF FIGURES

Figure 2.1: Conceptual Model 25

LIST OF ABBREVIATIONS

CBK: Central Bank of Kenya

M&A: Mergers and Acquisition

NPV: Net Present Value

NSE: Nairobi Securities Exchange

NYSE: New York Stock Exchange

ROA: Return on Assets

ROI: Return on Investments

UK: United Kingdom

VIF: Variance of Inflation

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Mergers and Acquisitions (M&A) undertakings have been on the rising trend due to the fact that they control agency problems. Sudarsanam (2013) noted that the principle motivation for undertaking M&A is to enhance the shareholders' esteem. In addition, the urge for competitiveness among business entities has led to corporate restructuring aimed at retaining competitive advantage hence improvement of the organizational financial performance (Lucey, 2015). Moreover, managers in organizations have been forced to reevaluate techniques of maximizing the shareholders returns; mergers and acquisitions is one such option. Consequently, this has prompted the increased mergers and acquisitions activities in the contemporary business environment aimed at improving the financial performance (Paul, 2014).

There are various theories explaining the need for M&A as a solution to the different challenges facing the business environment. This study focused on four theories; efficiency theory, agency theory, hubris theory and monopoly power theory. Efficiency theory explains that through M&A, a firm is able to transfer its superior operational, financial or managerial efficiency to the other combining firms; this increased efficiency in-turn ensures that the value of the firm is maximized. Agency theory argues that there exists a conflict of interest between managers and shareholders. Usually, managers are required to undertake decisions which focus on shareholders' wealth maximization. However, this is never

always the case since the managers have conflicting goals and aspirations. As such, managers will inevitably undertake activities which favor their interests much as this may not necessarily directly be of benefit to the shareholders. In addition, a company 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. Hubris theory was advanced by Roll (1986) and argues that managers often fail in effectively assessing merger feasibility due to exaggerated self-confidence leading to optimism errors. Monopoly theory on the other hand argues that the aim for M&A is to gain monopoly power (Nielsen, 1974).

Due to the benefits associated with M&A activities, commercial banks in Kenya have strongly embraced mergers and acquisitions. Some of the benefits associated with M&A include financial strength and cost reduction. Firms experiencing cash flow shortages may undergo mergers and acquisitions activities in order to increase their capital base and improve the financial strength hence improving the overall profitability and the financial performance (NSE, 2017).

1.1.1 Mergers and Acquisitions

A merger, according to Lucey (2014), is a business combination in which two firms in similar or separate business lines decide to join forces to improve operations. Acquisitions, on the other hand, are corporate pairings in which one company takes over the management and activities of another. For a merger to be successful, capabilities and expertise must be exchanged for cost effectiveness, synergy, and efficiency. In today's business environment, mergers and acquisitions are motivated by a variety of factors (Luypaert, 2016).

Mergers and acquisitions take place in three key forms; horizontal mergers, vertical mergers and conglomerate mergers. Horizontal mergers are as a result of a combination of firms that operate in the same industry; usually competitors offering similar goods or services (Martin, 2017). Marembo (2016) 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 inputs into the process of producing another product (David, 2019). Finally, conglomerate mergers occur between firms that produce unrelated products (Halpern, 215).

The reasons behind M&A are different for different organizations. Onyango (2016) indicated that the main motivations advanced for M&A are gaining market power, enhance innovation, and hence reduction of product development risks and efficiency maximization via economies of large scale production and increasing a firm's competitive advantage. Further, short term finance remedies are offered by M&A, challenges that may occur during the knowledge, reestablish new opportunities in a business so as to ensure the firm survive for a longer period in the future via advantages from synergies. Ndunyu (2018) concludes that M&A is a very important transformation factor to drive a business to prosperity. For M&A and synergies, there is a guaranteed success for a business.

Organizations that would like to expand their market share or diversify either their products or geographically need to choose between organic growth or growth achieved through mergers and acquisitions. Organic growth tends to be slow and steady because it takes time to setup business units and go through the growth process. Acquisitions tend to be preferred by firms which seek

accelerated growth and are ready to capitalize on opportunities. Ashley (2016) refers to M&A as a deliberate handover of control as well as ownership of an entity organized in one or more corporations.

The most common indicator of a successful M&A is that an acquisition enhances earnings per share. Shares are usually issued to buy a firm on a lower price-earnings multiple. Earnings are indeed boosted by a deal of M&A in the short term. However, in the long-term, the value is often lost, generally as a result of the acquiring management team being unable to enhance the target's value the way it anticipates. Companies whose owners are also managers of the firm tend to do better in regards to making successful acquisitions than those with isolated shareholders (Ashley, 2016).

The motivations for M&A strategy depend of the perspective of the entities involved and the reason for the M&A. An acquiring firm has different motivations when compared to a target firm being acquired. M&A’s are regarded as significant transformation agents and are an essential element of any business strategy. As the environment changes, the most innovative companies that are quick to respond are able to survive. Therefore, it is a significant strategic call for an enterprise to opt for merger and acquisition arrangements

1.1.2 Financial Performance

Financial performance deals with how prudently a company uses its assets to realize income (Ross, 1995). This is normally over a specified period of time; monthly, quarterly, semi-annually or annually. Measurement of financial performance is key to organizational success since all long term strategies are based on it. Financial performance is mostly determined by analyzing an organizations’ gearing ratios, profitability ratios and liquidity ratios. Liquidity ratios aim at

establishing whether a company will be able to finance its short-term commitments, gearing ratios sheds more light on the degree to which debt financing has been employed by a business entity because debt financing also attracts the finance charge inform of liquidity. Profitability ratios aim at establishing how well the business entities have efficiently managed the resources to achieve their goals. The major goal of any business entity is to minimize losses and maximize the profits. This will ensure business continuity of business entities. Firm's financial performance is determined from the financial statements. Financial statements entail the financial reports of business entities. Financial performance in this study was measured by return on assets (ROA). ROA is a profitability ratio that measures a firm's ability to generate revenues by efficient management of the assets at their disposal. With M&A comes the possibility of increase in total assets of the resultant firm therefore ROA was considered in this study as it reveals how efficiently the commercial banks are able to generate income by utilizing available assets. The ROA of the commercial banks pre-merger was then compared to the ROA of the commercial banks post-merger.

1.1.3 Mergers and Acquisitions and Financial Performance

According to financial synergy theory, M&A takes place since they generate synergy which in turn improves the financial performance (Roll, 1986). According to (CBK, 2017), M&A have enormously been of importance to performance of the commercial banks which have posted noteworthy financial performance contrasted with the banks which have not experienced M&A. The working collaboration between two or more combining firms is one of the major drivers of M&A which thus influences the financial performance. It has been recommended that administrative financial production, research or advertising can be achieved by any business entities by guaranteeing sound financial management systems. Business entities can

likewise accomplish their targets by M&A which can have extreme objective of financial collaboration (Sharma, 2014).

In order for any business element to remain financially stable, it must embrace merger obtaining procedures since it improves their financial performance (Sharma, 2014). Partners in any business setting have positive expectations from their venture and thus measure this from the financial performance. As indicated by the working collaborations hypothesis, M&A improves the profitability of businesses (Ross, 1986). A study by Santos et al. (2015) on effect M&A on firm value of insurance in UK came to conclude that M&A improved financial performance.

The main goal of M&A is to ensure that the business entities operate smoothly as a result of this restructuring process. There exists a direct relationship between mergers and acquisitions and the financial performance. Firms engaging in mergers and acquisitions will always want value creation for their shareholders. For the firms that have recorded failures resulting from M&A, the failures may be attributed to poor administrative leadership of the companies that were engaged in the deal (Myers, 2014). The financial performance of the companies is significant in the ultimate success or failure of mergers and acquisitions activities. Business entities normally engage in mergers and acquisitions when they feel the deal will be beneficial. Many theories which have been advanced in the area of mergers and acquisitions have confirmed the existence of the relationship between mergers and acquisitions and financial performance. The theory of economics argues that mergers and acquisitions exist to lower operational costs consequently affecting the financial performance.

1.1.4 Commercial Banks in Kenya

As at January 2020 the total number of commercial banks in Kenya stood at 42. In the year 1989, Kenya recorded the first merger of commercial banks where nine banks came together to form a resultant bank that is known today as the Consolidated Bank of Kenya. It has since seen 33 banks merge and 6 have been acquired in the Kenyan banking sector. Some of the most recent mergers include NIC Group PLC and Commercial Bank of Africa Ltd which merged in 2019 to form NCBA Bank Kenya PLC, City Finance Bank Limited and Jamii Bora Bank which merged in 2010 to form Jamii Bora Bank Limited. Kenya Commercial Bank and Savings and Loan merged in 2010 to form KCB Bank Limited. In 2008, CFC Bank merged with Stanbic Bank Limited to form CFC Stanbic Bank Limited in 2008 (CBK, 2020).

The most recent acquisitions include the acquisition of National Bank of Kenya Ltd by KCB Group PLC in 2019, acquisition of Giro Commercial Bank Ltd by I&M Bank Ltd in 2017, Fidelity Commercial Bank Ltd by SBM Bank Kenya Ltd in 2017, Guaranty Trust Bank PLC acquired Fina Bank in 2010 to form Guaranty Trust Bank (Kenya) Limited (CBK, 2020). The increase of the minimum core capital requirements by the Central Bank of Kenya has been a major motivation of M&A’s in Kenya. Commercial banks have also merged in a bid to improve profitability through the raising of their market share (Njangiru & Ondieki, 2015)

1.2 Research Problem

According to a recent global survey, M&A activities worldwide have been used as alternative models in highly competitive sectors for conducting business with an aim of enhancing financial performance. As of July 2017, the total number of M&A stood at approximately 2.03 billion (Jack, 2017). This has been attributed to high competition in the business environment forcing

firms to adopt new business models. The greatest positive benefits of M&A activity have come because every firm has become a potential takeover target and the activity is aimed at improving the financial performance. M&A’s give the firms in the merger competitive advantage due to the synergies generated and thus ultimate improvement of the value of the merged firms (Fluck & Lynch, 2014).

In Kenya, a great number of M&A activities witnessed among commercial banks have been attributed by the fact that banks which have adopted M&A activities have exhibited improved financial performance. This has been due to the benefits associated with synergy. Synergy is a strategy that ensures that the combined power of two business entities exceeds the previously separate entities (CBK, 2017). Because commercial banks are a vital part of the financial sector and the economy, mergers and acquisitions are critical to the financial performance of numerous organizations, particularly commercial banks. M&As have an impact on financial performance through boosting shareholder value, increasing profitability, assuring optimal resource usage due to economies of scale, and raising return on equity for firms (Wangari, 2015).

Numerous studies have been carried out in the area of M&A’s which have yielded mixed and inconclusive results pertaining to effects of M&A’s on performance of various firms. Friesen (2015) 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 (2015) 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 (2016) studied 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. This study however employed the Altman's discriminate model while this current study utilizes paired sample test to bridge the methodological gap.

Marangu (2017) argued that there was significant performance improvement of the non-quoted insurance firms which were attributed to merging as opposed to the non-quoted insurance companies that had not merged within the same period.

Kiprotich (2017) studied the relationship between M&A on value of listed insurance companies and concluded that mergers and acquisition have no relationship that is significant statistically to the performance however positive. This study exhibited a contextual gap since it focused on listed insurance companies while the current study focuses on commercial banks.

Mwanza (2016) undertook a research in Kenya on M&A and performance of insurance firms. The conclusion from the study was that M&A enhances financial performance of the merged firms. However, the study by Mwanza (2016) considered data for M&A two years prior the merger and two years financial performance data after the merger which may be too short for one to observe the financial performance of a firm and make conclusions. A contextual gap is exhibited in this study.

In conclusion, the major limitations from the previous studies were existence of contextual and methodological gaps and a few studies have been extensively carried out on Kenyan commercial banks during the 10 year period that this study will focus on between 2008 and 2018; a period that has witnessed a surge of M&A in the Kenyan banking sector that has seen 10 commercial banks merge and 5 commercial banks acquired (CBK, 2020). This informs the need for the current study which aimed at establishing the effect of M&A on financial performance of commercial banks in Kenya?

1.3 Research Objective

To determine the effect of M&A on the financial performance of commercial banks in Kenya.

1.4 Value of the Study

The significance of the study cannot be overemphasized. This study will assist scholars and academicians to pursue further studies and add literature to M&A and performance of institutions. Additionally, the study would also help customers of the banks which have embraced M&A to gain an understanding on the difference in financial performance before and after M&A. This study would further help the government in understanding how the banks are able to operate with and without M&A and make related fiscal decisions. Finally this study would help policy makers in making policies with regard to commercial banks that undergo mergers and acquisitions.

This research would be helpful to the investors with the insight on mergers and acquisitions to make the decisions on the investment. It would provide them with information to help them make investment choices of the stocks of the profitable commercial bank. The central bank of

Kenya would borrow from this research in making informed policies aimed at maintaining the financial stability within the financial markets.

The study would 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 will assist both the management and the shareholders with information that will assist in predicting and ensuring good timing for the M&A’s.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter covers the theories that anchored the study to its objective, it also covers the insight of the previous literature and studies undertaken in line with the topic of the study in question.

2.2 Theoretical Review

This study is anchored on four major theories. The theories are; efficiency theory, agency theory, hubris theory and monopoly theory and are detailed in the subsequent paragraphs.

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.

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.

The financial stability of a company depends on its resources. Company resources are grouped into three categories; tangible resources, human capital and organizational capital. Many organizations generate competitive advantage through these resources hence improving their financial performance. Since these resources can neither be copied nor substituted, companies opt for mergers and acquisition activities to access the resource hence get significant synergies.

2.2.2 Agency Theory

This theory was propelled by Jensen and Meckling in 1976 but was originally from studies conducted by Berle and Means (1932). This theory describes managers as 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 maximize 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 maximize the available firm resources within the limited time frame.

Mueller (1969) posits that business entity managers prefer M&A for their own benefits as opposed to maximization of shareholders' wealth. The authority and prestige of the managers derived from their occupations are directly related to growth of the company rather than its profitability. Investors and shareholders of in any organization expect the management team to adopt strategies which maximize their value. However, in many incidences, their expectations are not met given their minimal capability of tracking the managers' activities due to financial constraints.

According to the agency theory's value lowering approach, organizations are at a disadvantage when it comes to realizing the benefits of synergies established through M&As (McDonald, Westphal and Graebner, 2008). The key disadvantages that firms face include a lack of resources to identify targets that can benefit them, an inability to welcome other cultures, and a lack of experience managing M&A's in a way that maximizes the firm's profits.

The decision making activities and control of business organization are positively related to its financial performance. Managers most often than not try to maximize their wealth by awarding themselves huge salaries at the expense of shareholders, who are the owners of the business entities, hence adversely affecting the financial performance of firms (Mueller, 1969). Additionally, management may undertake transactions which diversify the company portfolio hence minimizing the bankruptcy risk to secure their jobs. Theory emphasizes the manager's motives of undertaking M&A for their own interest.

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 may be defined as an agency issue brought about by the separation of ownership and control leading to disputing interests between the managers and shareholders.

Empirical 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 frame1963 -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

2.2.4 Monopoly Theory

According to Nielsen (1974) mergers and acquisitions activities are planned and executed by companies in a competitive sector to gain monopoly power. A company operating in losses can be acquired by a financially stable company and the resultant firm will have a monopoly power by gaining the greatest market share as well as controlling the market. Monopoly is a price setter hence the firm can predict the expected profits over a given period. According to the monopoly theory, M&A activities are aimed at dictating the market operations.

The ability of a company to control market activities gains the market power. The monopoly theory has been rejected by a number of theorists since there is indirect evidence of mergers on

market monopoly. According to this theory the motive for M&A is the criterion of monopoly power (Lambert, 2001). Monopoly power means the market structure is controlled by one seller who sells unique products to its customers and that he faces no competition from other sellers. Under this market, no restrictions or barriers and by mergers and acquisitions, separate companies can be considered to become a bigger company which will own and control all the market. Monopoly power will benefit the listed companies.

The monopoly theory avers that mergers are formed as a way of creating monopoly and subsequently increased market power through dominance. This is the proper characterization of conglomerate or horizontal mergers. Market dominance can be realized either by the intentional restriction of products, restricting market entry for potential entrants and cross-subsidizing products (Rodermann, 2004; Trautwein, 1990).

According to monopoly theory the motive for mergers and acquisitions is the creation of monopoly power (Lambert, 2001). Monopoly power means the market structure is controlled by one seller who sells unique products to its customers and that he faces no competition from other sellers. Under this market, no restrictions or barriers and by mergers and acquisitions, separate companies can be considered to become a bigger company which will own and control all the market. This theory is relevant to this study since it encourages monopoly power which can be attained through mergers and acquisitions. Monopoly power will benefit the commercial banks by improving their share return as a result of increased profitability

2.3 Determinants of Financial Performance

This section provides insights behind the literature and studies carried out by earlier by scholars in determining M&A and performance. Financial performance is determined by; leverage, external factors, management efficiency and profitability.

2.3.1 Leverage

Leverage refers to fraction of debt to equity capital of a firm. There have been point by point impacts of the two on the firm's value and cost of capital (Pandey, 2016). Financial performance of a specific company is dictated by its due obligation of a similar firm. Jensen (1986) contended that the moral hazard conduct is diminished throughout financing by decreasing income at the managers' disposal hence expanding the pressure to perform and this enhances the performance of the firm monetarily.

Thus, a firm with high leverage is in great position to fiscally perform better. Extant researches dealt with the connection between leverage and performance of the firm and came to conclusion that high leverage diminishes the conflict amongst managers and shareholders leading to increase in performance and eventually a positive relationship develops (Lucey, 2015).

2.3.1 Liquidity

This is the extent of buying or selling securities and not affecting the price of the asset (Desai, 1980). It is measured using acid test ratio and current ratio. Current ratio tells us about those assets that can be liquid within 1 year and the liabilities that will be due for payment. Acid test ratio on the other hand is about the availability of sufficient resources that are easily convertible to cash for the purpose of catering for the current liabilities. Firms with more liquid assets

normally outperform the companies with less liquid assets because cash is readily available to cater for their needs at any point in time. The degree to which assets can be purchased or sold is known as liquidity. These transactions do not affect the price of the assets in the market. The quick ratio informs us on the fulfillment of the short term obligations as they fall due using the most liquid cash excluding the inventories. It is the ratio of current assets minus inventory divided by current assets. Current ratio on the other hand tells us more about the assets which will become liquid within 12 months with the liabilities to be settled. Business entities with greater percentage of liquid assets normally perform better because cash is readily available to cater for the obligations (Wood, 1988).

2.3.3 Management Efficiency

Johnson (2005) is on the opinion that management efficiency is a situation where an organization utilizes its resources prudently in order to maximize on its productivity level. Management efficiency is concerned with reducing resources waste with an aim of maximizing the firms' output level. In addition, management efficiency is aimed at increasing the efficiency of an organization's operations through sharing of duties whereby chief executive officer can as well act as a managing director. Management efficiency is measured by proxy of management ratio measuring the operating expenses to sum of entity's assets. The higher the proxy management ratio, the greater the financial performance. The efficiency of management is a major aspect that supports performance of any firm. This is signified by various financial ratios such as earnings growth rate, total asset growth and loan growth rate. Management's performance is habitually articulated qualitatively through prejudiced assessment of administration structures, managerial control, regulatory rules, and work force superiority, among others. Nonetheless, a number of monetary ratios of the financial statements operate as a substitute for organizational competence.

Management' ability to organize its funds competently, maximizing outputs, and lessening the operational expenditures can be calculated using financial ratios. One of these ratios can gauge excellence of the management in operating profits to income ratio (Sangmi & Nazir, 2010). A high operating profit to overall income is a reflection of competent organization in relations of functional effectiveness as well as generation of incomes.

2.3.4 Firm Size

Burca and Batrinca (2014) asserts that the size of the firm affects its financial performance negatively or positively. Firms that have a large asset base have the advantage of obtaining services much faster than small firms due to their purchasing strength hence ability to undertake production and distribution cheaply, due to economies of scale. With this advantage, the larger firms are in a better position to spread their risks. Such firms are also able to respond swiftly to any risk arising from the environment and the market.

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

Thomson, (2010) did a study on share price reaction to acquisition announcement in N Y S E. The study aimed to establish the influence of acquisitions on shares value reaction of the entities quoted at the market. 102 firms were sampled from the 200 firms quoted at the market. Secondary data was used and their findings revealed that stock prices rose a few days preceding the acquisitions pronouncement.

Mohamed et al., (2011) did a study on the influence of mergers and acquisitions on the financial situation of companies in India from 2001 to 2008. 182 firms trading at the Bombay securities market were selected. However, due to time and resource constraints 91 firms were selected as a sample for the study. Linear regression model was used for analysis. Secondary data for companies for analysis was used. Dividend per share and earnings per share was determined over a four years period prior and a similar period after the merger and acquisition. From the findings, the financial performance of those companies improved after mergers and acquisitions.

Jamal & Malik, (2013) did a study about the influence of consolidations on the financial performance of Pakistan banks between 2005 and 2011. All the 157 listed commercial banks were selected for the study. However, 70 banks which had undergone mergers and acquisitions were selected as a sample for study. Data from the published audited accounts from the banks was used. Linear regression model was used in the analysis. Dividend per share and return on assets were determined three years prior merging and acquisition and three years post merging or acquisition. From their findings, these forms of business undertakings had insignificant influence on the financial behavior of the commercial of Pakistani banks.

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&A' 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.

Louz (2016) conducted a study in Greece pertaining M&A and performance. He selected a sample of 130 individual respondents. This study was done over a duration of seven years between 2007 and 2014. His total population constituted 281 firms. He carried out his analysis for a period of three years before mergers and three years after mergers. The performance in financial terms was measured by ROE. Regression analysis was also employed. Methodology used was appropriate. He concluded that M&A had a negative effect on the financial performance.

2.4.2 Local Studies

Kauki, (2011) did a study on the effect of mergers on the financial performance of commercial banks trading at the NSE from 2006 to 2010 in Kenya. A sample of 8 commercial banks which had undergone mergers was selected. Secondary data from the published financial statements of the commercial banks in Kenya was used. Data was analyzed three years after mergers and three years before mergers. Financial performance measurement ratios which included dividend per share and earnings per share were computed and compared. The study also employed the linear regression model in the analysis. From his findings, the financial performance of commercial banks greatly improved after mergers.

Rono, (2012) carried out a study on how merging and acquisitions of construction and manufacturing companies influenced their financial position in Kenya between 2003 & 2010. The population of interest was 13 construction and manufacturing companies which had undergone mergers and acquisitions. A sample of 7 construction and manufacturing companies was selected for analysis. The model used for analysis was linear regression model. Key indicators like ROA and ROE were computed and compared. She concluded that financial behavior of construction and manufacturing companies improved after mergers and acquisitions.

Kasinwa (2015) carried out a study on the effect of M&A on financial performance of organizations listed on the NSE. In her research, descriptive research design was used in the study of the sample of 20 listed firms at the NSE in the five years between 2010 and 2014. The study used secondary data available for all firms at the NSE. The study found a negative relationship between M&A and financial performance. Subsequently it concluded that there's was a negative correlation between M&A and financial performance for firms listed at the NSE.

Kimeu, (2015) sought to understand how merging of firms influences the financial behavior of the oil marketing firms in Kenya between 2008 to 2013. A sample of 10 oil marketing firms were selected. Secondary data was then extracted from the respective firms' financial statements and employed in the study. Financial performance was measured by return on assets, return on equity and dividend per share for the oil marketing firms. Linear regression model was employed for analysis. From the study findings, the oil marketing firms underperformed after mergers.

Kusa (2017) study looked at the effect of M&A on the financial performance of oil marketing firms in Kenya in the period 2010-2016. A sample of Eight (8) oil marketing companies were selected from a population of fourteen (14) marketing companies for the study. The study used secondary data to compare the 3years pre mergers and 3years post merger financial performance. Linear regression model was also employed. He concluded that M&A have a positive effect on the financial performance of oil marketing firms in Kenya.

Farhatali (2017) study looked at the effect of M&A on the financial performance of non-listed banks in Kenya. 2009-2015 was the study period for the study. 8 non-listed Commercial banks were selected from the population of 14 banks as the sample of the study. The study used the secondary data to compare the 3 years pre mergers and 3years post mergers. He concluded that M&A did not have any effect on the financial performance.

2.5 Conceptual Framework

The research will analyze the effect of M&A on the financial performance of the banks in Kenya. The independent variable of the study will be mergers and acquisitions while the dependent variable will be financial performance.

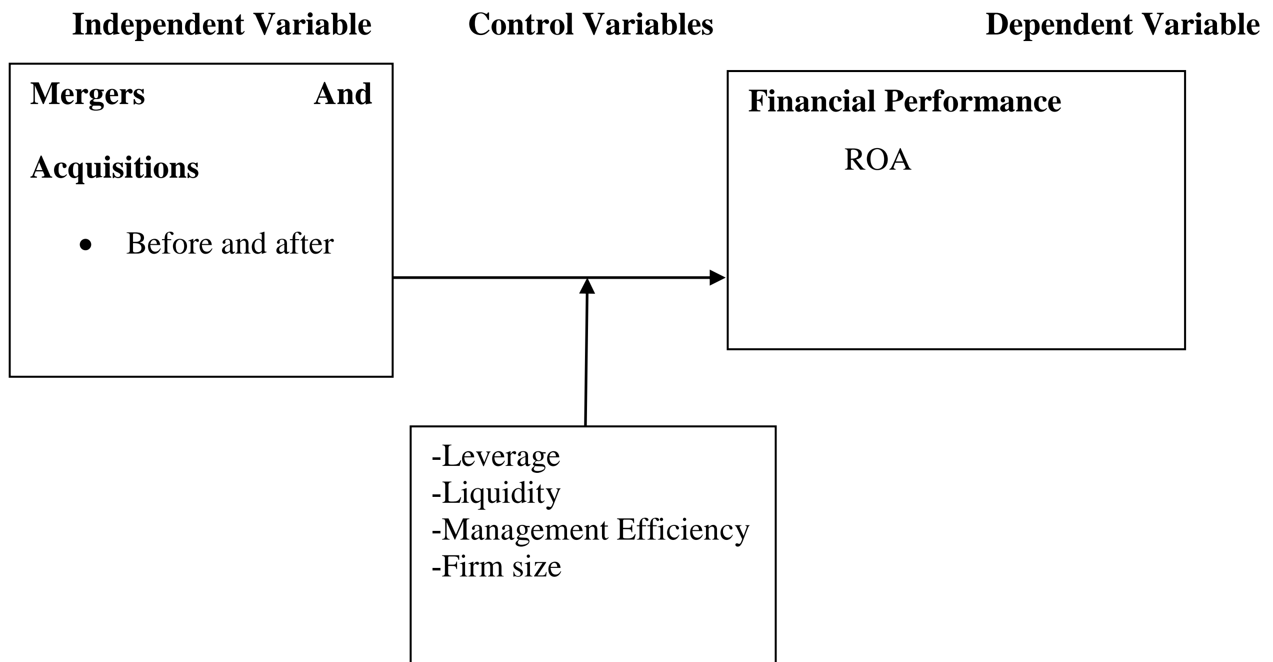

Figure 2.1: Conceptual Model

2.6 Summary of Literature Review

Theoretical and empirical literature have been examined in this chapter. Various theories on mergers and acquisitions have been discussed as well as a presentation of empirical studies by previous researchers examined. The various empirical studies examined yielded mixed and inconclusive results. Some of the studies revealed that the firms studied recorded better financial performance in the period subsequent to the mergers. On the other hand, some studies found that there was insignificant growth if any on the institutions financially subsequent to the mergers. Osoro, (2010) carried out a study on the impact of M&A of firms on the financial situation of insurance firms in the country between 2001 to 2007. While other findings can confirm a positive impact of the Mergers &Acquisitions, others concluded that mergers and acquisitions

had insignificant effect on the financial performance. It is with this backdrop that this research is being carried.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This section covers the methodology that was utilized in this research. Methodology describes research design, technique of collecting data, target population, method and data analysis employed in the study.

3.2 Research Design

It provides a framework on how the study was carried out. Research design outlines the guideline to be employed on data collection, the analysis of the data and interpretation of the results (Basic Research Concepts, 2014). This entails methodology adopted in conducting the research work (Cooper, 2006). Descriptive research design was used. Descriptive studies show the relationship that is between objectives hence describing the population that is being studied (Basic Research Concepts, 2014). In this case, the study was meant to analyze M&A and performance of commercial banks in Kenya.

3.3 Study Population

Laurel (2003) refers to a population as all the items that have specific characteristics and that are of interest to the researcher from which a generalization can be formed from the data collected. A population consists of a set of homogeneous elements that are being studied. All the 20 commercial banks that engaged in M & A activities over the study period formed the population of study. All banks in Kenya which had undergone M&A between 2008 to 2018 (20 banks) were analyzed.

3.4 Data Collection

The research utilized secondary data which was sourced from financial statements of the commercial banks between 2008 and 2018. Secondary data obtained from Capital Markets Authority of Kenya and from Central Bank of Kenya was used. Secondary data collected was that of long-term debt, total assets, current liabilities, current assets and return on assets Analysis was done three years before M&A and three years after M&A.

3.5 Data Analysis

Descriptive and inferential statistics were utilized in analyzing the collected secondary data. Descriptive statistics comprised the mean and the standard deviation which helped in summarizing the research data. This research used long term debt, total assets, current assets, current liabilities and ROA in the analysis. Data was analyzed 3 years before mergers and acquisitions and 3 years after mergers and acquisitions to assess whether M&A have any significant effect on the financial performance.

3.5.1 Diagnostic Tests

Diagnostic tests were employed in the study to ascertain the reliability of the outcome. Normality, Autocorrelation and Multicollinearity tests were run. Normality is a test of assumption that the residuals of the response variable are normally distributed around the mean. This was determined by Kolmogorov-Smirnov Test and the Shapiro-Wilk Test. Autocorrelation test was performed using Durbin-Watson. Where the statistic is less than two there is positive autocorrelation and where greater than two there is negative autocorrelation. To ensure the data collected is free from biasness and that independent variables are not related to each other, the study conducted a multicollinearity test. The

variance of Inflation was used to test multicollinearity. Whenever the values of VIF is between 1 and 10, then there is no multicollinearity while when the VIF is less than 1 or greater than 10, then there is presence of multicollinearity. When the test fails one should standardize the continuous variables by choosing on a standardization method on the regression dialog box.

3.5.2 Analytical Model

To establish the relationship among the different variables in the study, a paired t-test at 5% significance level was conducted. The paired T-test was used to analyze the data before M&A and after M&A and then the paired samples t test was employed as the analytical model for the study. The formulae is as shown;

$$Paired\ t - test = \frac{x - \mu}{\sqrt[s]{n}}$$

Where;

x = Population mean,

μ = t critical value,

S=Sample mean and

n= Sample size

3.5.3 Tests of Significance

In order to establish the degree of influence of independent variables on dependent variable, the researcher carried out an F- test. The confidence level of significance of at which variables were interpreted were assumed at 95%. Interpretation of results took the following assumption; a variable containing 0.05 of p-value or less value was regarded as being significant whereas p-value of above 0.05 was regarded as not significant.

CHAPTER FOUR

DATA ANALYSIS AND FINDINGS

4.1 Introduction

This section majors on the analysis of the data collected from the various sources including company financial reports and CBK annual reports in establishing the influence of M&A on the financial performance of commercial banks in Kenya by employing descriptive statistics, T-test analysis, the findings were presented in table forms as described in subsequent sections.

4.2 Descriptive Statistics

This section shall present the descriptive results of the research during pre and post-merger, measures of central tendency, the trends analysis including commercial banks average ROA, leverage ratio, liquidity, management efficiency and firm size as logarithm of total assets.

4.2.1 ROA

Table 4.1: Descriptive Statistics of ROA

	Pre-Merger		Post-Merger	
	Mean	**Std. Deviation**	**Mean**	**Std. Deviation**
KCB	0.047	0.066	0.096	0.020
Savings and Loan	0.036	0.050	0.096	0.020
Prime Capital credit	0.043	0.003	0.037	0.008
Prime Bank	0.033	0.003	0.037	0.008
CFC Bank	0.097	0.018	0.200	0.041

Stanbic Bank	0.074	0.014	0.200	0.041
City Finance Bank	0.095	0.020	0.105	0.022
Jamii Bora	0.063	0.014	0.105	0.022
Eco Bank Ltd	0.113	0.043	0.124	0.026
EABS Bank Ltd	0.120	0.032	0.124	0.026
Guaranty Trust Bank PLC	0.176	0.028	0.147	0.031
Fina Bank	0.134	0.021	0.147	0.031
DBT	0.121	0.021	0.136	0.028
Fina Bank	0.092	0.015	0.136	0.028
SBM Bank Kenya Ltd	0.369	0.013	0.478	0.098
Fidelity Bank Ltd	0.280	0.010	0.478	0.098
I&M Bank	0.213	0.010	0.242	0.050
Giro Bank	0.162	0.008	0.242	0.050
Equitorial Commercial Bank	0.097	0.026	0.159	0.033
Southern Credit Banking Corporation	0.073	0.020	0.159	0.033

On analysis of the companies' ROA before and after merger, it was established that all the M & A yielded an increase in ROA except for Prime Capital credit and Guaranty Trust Bank PLC. SBM Bank Kenya Ltd recorded the highest increase in ROA of 0.478 after the merger. Prime Bank ltd recorded the lowest ROA of 0.003. It is clear from the results in Table 4.1 that merger and acquisition leads to the rise of ROA among commercial banks in Kenya.

4.2.2 Leverage

Table 4.2: Descriptive Statistics of Leverage

	Pre-merger		Post-Merger	
	Mean	**Std. Deviation**	**Mean**	**Std. Deviation**
KCB	0.062	0.043	0.096	0.020
Savings and Loan	0.076	0.053	0.096	0.020
Prime Capital credit	3.828	0.272	3.260	0.377
Prime Bank	4.643	0.329	3.260	0.377
CFC Bank	4.214	0.065	4.032	0.063
Stanbic Bank	5.111	0.080	4.032	2.307
City Finance Bank	5.655	0.419	4.200	0.533
Jamii Bora	6.859	0.508	4.200	0.533
Eco Bank Ltd	4.611	0.829	4.120	0.468
EABS Bank Ltd	5.593	1.005	4.120	0.468
Guaranty Trust Bank PLC	10.844	8.054	22.548	4.534
Fina Bank	13.154	9.768	22.548	4.534
DBT	5.312	0.768	7.860	1.047
Fina Bank	6.444	0.931	7.860	1.047
SBM Bank Kenya Ltd	5.874	0.940	9.380	1.131
Fidelity Bank Ltd	7.125	1.140	9.380	1.131
I&M Bank	6.429	1.231	7.046	0.729
Giro Bank	7.799	1.493	7.046	0.729
Equitorial Commercial Bank	5.414	0.185	4.923	0.535

Southern Credit Banking Corporation	6.567	0.224	4.923	0.535

Table 4.2 shows leverage ratio of commercial banks before merge and post-merger. On analysis of the companies' leverage ratios before and after the merger and acquisition, it was established that Guaranty Trust Bank, SBM Bank Kenya Ltd and Fidelity Bank Ltd recorded a notable increase in the leverage after merger and acquisition. On the contrary, Kenya Commercial Bank Ltd recorded an insignificant increase after merger. The leverage ratio for Prime Bank ltd, CFC Stanbic Bank ltd, Jamii Bora Bank ltd, Eco bank Kenya ltd and Spire Bank dropped drastically after merger.

4.2.3 Liquidity

Table 4.3: Liquidity Descriptive Statistics

	Pre-merger		**Post-Merger**	
	Mean	**Std. Deviation**	**Mean**	**Std. Deviation**
KCB	1.901	0.018	2.491	0.553
Savings and Loan	1.502	0.014	2.491	0.553
Prime Capital credit	1.771	0.015	2.299	0.510
Prime Bank	1.399	0.012	2.299	0.510
CFC Bank	2.314	0.455	3.364	0.746
Stanbic Bank	1.828	0.360	3.364	0.746
City Finance Bank	2.872	0.022	3.732	0.827
Jamii Bora	2.269	0.018	3.732	0.827
Eco Bank Ltd	2.654	0.044	3.486	0.773

EABS Bank Ltd	2.096	0.035	3.486	0.773
Guaranty Trust Bank PLC	2.698	0.022	3.510	0.778
Fina Bank	2.131	0.017	3.510	0.778
DBT	2.776	0.010	3.557	0.789
Fina Bank	2.193	0.008	3.557	0.789
SBM Bank Kenya Ltd	2.791	0.026	3.648	0.809
Fidelity Bank Ltd	2.205	0.020	3.648	0.809
I&M Bank	1.301	0.147	1.730	0.384
Giro Bank	1.028	0.116	1.730	0.384
Equitorial Commercial Bank	2.404	0.078	3.156	0.700
Southern Credit Banking Corporation	1.900	0.062	3.156	0.700

Table 4.3 shows liquidity of commercial banks before and after merger. An analysis of the companies' liquidity before and after merger established that the average liquidity ratio for all the commercial banks improved after merger. Jamii Bora bank posted the greatest increase in liquidity after merger. This was followed closely by SBM Bank Kenya Ltd and Diamond Trust Bank Kenya Limited respectively. The results are an indication that merger and acquisition improves the liquidity state of the commercial banks.

4.2.4 Management Efficiency

Table 4.4: Management Efficiency

	Pre-merger		**Post-Merger**	
	Mean	**Std. Deviation**	**Mean**	**Std. Deviation**

KCB	0.475	0.005	0.623	0.138
Savings and Loan	0.319	0.003	0.623	0.138
Prime Capital credit	0.443	0.004	0.574	0.127
Prime Bank	0.297	0.003	0.574	0.127
CFC Bank	0.604	0.070	0.841	0.186
Stanbic Bank	0.405	0.047	0.841	0.186
City Finance Bank	0.718	0.005	0.933	0.207
Jamii Bora	0.481	0.004	0.933	0.207
Eco Bank Ltd	0.663	0.011	0.872	0.193
EABS Bank Ltd	0.445	0.008	0.872	0.193
Guaranty Trust Bank PLC	0.675	0.005	0.877	0.195
Fina Bank	0.452	0.004	0.877	0.195
DBT	0.694	0.003	0.889	0.197
Fina Bank	0.465	0.002	0.889	0.197
SBM Bank Kenya Ltd	0.698	0.007	0.912	0.202
Fidelity Bank Ltd	0.468	0.004	0.912	0.202
I&M Bank	0.325	0.037	0.432	0.096
Giro Bank	0.218	0.024	0.432	0.096
Equitorial Commercial Bank	0.502	0.073	0.700	0.155
Southern Credit Banking Corporation	0.336	0.049	0.700	0.155

Table 4.4 illustrates commercial banks management efficiency before and after merger. The results indicate that management efficiency improved for all the commercial banks post-merger.

4.2.5 Firm Size

Table 4.5: Firm Size Descriptive Statistics

	Pre-merger		Post-Merger	
	Mean	**Std. Deviation**	**Mean**	**Std. Deviation**
KCB	11.702	0.055	12.474	0.657
Savings and Loan	4.328	0.041	12.474	0.657
Prime Capital credit	5.312	0.044	6.895	1.529
Prime Bank	4.032	0.033	6.895	1.529
CFC Bank	7.439	0.508	10.093	2.238
Stanbic Bank	5.646	0.385	10.093	2.238
City Finance Bank	8.616	0.066	11.196	2.483
Jamii Bora	6.539	0.050	11.196	2.483
Eco Bank Ltd	7.961	0.132	10.459	2.320
EABS Bank Ltd	6.042	0.100	10.459	2.320
Guaranty Trust Bank PLC	8.094	0.065	10.529	2.335
Fina Bank	6.143	0.049	10.529	2.335
DBT	8.327	0.031	10.671	2.366
Fina Bank	6.320	0.023	10.671	2.366
SBM Bank Kenya Ltd	8.374	0.077	10.944	2.427
Fidelity Bank Ltd	6.355	0.058	10.944	2.427
I&M Bank	3.903	0.441	5.189	1.151

Giro Bank	2.962	0.334	5.189	1.151
Equitorial Commercial Bank	4.428	0.554	6.137	1.361
Southern Credit Banking Corporation	3.361	0.420	6.137	1.361

Table 4.5 illustrates commercial banks size in terms of asset base before and after merger. The results indicated that the average total assets grew for all the commercial banks post-merger. Kenya Commercial Bank Ltd, Jamii Bora Bank ltd and Eco bank Kenya ltd registered the largest growth in total assets after the mergers. CFC Stanbic Bank ltd followed closely. This implies that firm size as a logarithm of total assets improves for commercial banks post-merger.

4.4 Diagnostic Tests

Diagnostic tests employed by this study were normality test, multicollinearity test, autocorrelation and homoscedasticity tests.

4.4.1 Normality Tests

Shapiro-Wilk test was appropriate for this study in testing normality. The null hypothesis was null as shown below and an alternative hypothesis.

H_0=the secondary data was not normal

H_1= the secondary data was normal

A recorded p-value that is more than 0.05 will lead to a null hypothesis rejected and the vice versa would be true. These results are shown in the table 4.2 below.

Table 4.6: Shapiro-Wilk Test of Normality

Variables	Kolmogorov -Smirnov[a]			Shapiro -Wilk		
	Statistic	Df	Sig.	Statistic	Df	Sig.
ROA	.288	19	.331	.747	19	.401
Leverage	.364	19	.331	.656	19	.401
Liquidity	.309	19	.331	.742	19	.401
Management efficiency	.329	19	.331	.703	19	.401
Firm size	.349	19	.331	.616	19	.401

Source; Researcher (2021)

In accordance to the results, the Shapiro-Wilk values were 0.401 for ROA, Leverage, Management efficiency, Liquidity and firm size each. Kolmogorov-Smirnov tested significant values were at 0.331 for ROA, leverage, management efficiency, Liquidity and firm size each. The data recorded a p-value that was more than 0.05 and thus the null hypothesis was rejected while the alternative hypothesis being the normality test showed the normal distribution. Therefore, this data could be used in guiding the parameter test like the analysis of variance, persons' and regressions analysis respectively.

4.4.2 Homoscedasticity Test

For homoscedasticity, Breusch-Pagan test was utilized. This is normally applied when there is a normal distribution in the error terms. The constant variance is a null hypothesis of the test. There is a rejected hypothesis the p-value becomes significant and this is true when the variance is not constant. The information below shows that the error term is constant because the p-value is greater than 0.05.

Table 4.7: Test for Heteroscedasticity

Breusch -Pagan / Cook -Weisberg test for heteroscedasticity		
Ho: Constant variance		
Variables: fitted values of net profit		
chi2 (1)	=	1.34
Prob> chi2	=	0.2476

Source; Researcher (2021)

Basing on the level of output, the values obtained were greater than 0.05, hence there is no significant difference existing in the variation of dependent to independent variables that were tested.

4.4.3 Multicollinearity Test

Multicollinearity is said to be present where the there is more than one relationship is liner in some situation. Multicollinearity is referred to a situation where the variables have a high correlation. This study applied multicollinearity to its data. The value of variables on VIF was also applied in this study. If the value of VIF is below 10 then the results indicate that there is no multicolinearity or non-existence. The result recorded a less than 10 value hence no multicolinearity. This result is shown on the table 4.8 below in Table 4.8.

Table 4.8: Multicollinearity Test

	Colinearity Statistics Tolerance	VIF
ROA	..500	2.000
Leverage	.608	1.646
Liquidity	.633	1.580

Management efficiency	.493	2.027
firm size	.242	2.083

Source; Researcher (2021)

4.4.3 Test of Stationarity

A summary of the results is shown below where Augmented Dickey Fuller test was employed. All the values at 1% where recorded showing that the confidence was good having considered all the trends missing and gaps.

Table 4.9: Serial Correlation

	Test Statistics	**1% Critical Value**	**5% Critical Value**	**10% Critical Value**	**Sig.**
ROA	-3.311	-2.457	-1.697	-1.31	Stationary
Leverage	-2.152	-2.457	-1.697	-1.31	Stationary
Liquidity	-2.304	-2.457	-1.697	-1.31	Stationary
Management efficiency	-3.301	-2.457	-1.697	-1.31	Stationary
Firm size	-3.51	-2.457	-1.697	-1.31	Stationary

Source; Researcher (2021)

4.4 Paired Samples Test

The study employed the paired samples t-test to assess the presence of a statistically significant variance linking financial performance before and after the merger and acquisitions. The paired samples statistics were carried out for abnormal returns (AR), average abnormal returns (ARR) and the cumulative average abnormal returns (CAAR) respectively. The results were as follows

Table 4.10: Paired Samples Test

	Paired Differences							
				95% Confidence Interval of the Difference				
	Mean	Std. Deviation	Std. Error Mean	Lower	Upper	t	Df	Sig. (2-tailed)
Pre-merger ROA – Post-merger ROA	.04360	.06062	.01356	.07197	.01523	3.216	19	.005
Pre-merger leverage – Post-merger leverage	.89752	.69031	.82518	2.62464	.82960	3.088	19	.007
Pre-merger liquidity– Post-merger liquidity	.99555	.34200	.07647	1.15561	.83548	13.018	19	.000
Pre-merger management efficiency– Post-merger management efficiency	.28134	.11724	.02622	.33621	.22648	10.732	19	.000

Pre-merger firm-size – Post-merger firm size	2.964141.10915	.24801	3.48324	2.44505	11.952	19	.000

From the analysis the findings clearly show that before the merger and acquisition average ROA mean difference was 0.0436 with a standard deviation of 0.06062. The p value is 0.005 <0.05 and therefore it can be concluded that ROA has a statistic change significantly before and after mergers and acquisition. 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.

The study also revealed that the merger and acquisition average mean difference leverage ratio was 0.89752 with a standard deviation of 0.69031. The p value is 0.007 <0.05 and it can be concluded that leverage has a statistic change significantly before and after mergers and acquisition. In addition, the study revealed that the merger and acquisition average mean difference liquidity ratio was 0.99555 with a standard deviation of 0.34200. The p value is 0.000 <0.05 and therefore it can be concluded that liquidity has a statistic change significantly before and after mergers and acquisition.

Further the study revealed that the merger and acquisition average mean difference of management efficiency was 0. .28134 and a standard deviation of 0.11724. The p value is 0.000

<0.05 and therefore it can be concluded that management efficiency has a statistic change significantly before and after mergers and acquisition. Finally, the study revealed that the merger and acquisition average mean difference of firm size was 2.96414 with standard deviation of 1.10915. The p value is 0.000 <0.05 and therefore it can be concluded that firm size has a statistic change significantly before and after mergers and acquisition.

4.5 Correlation Analysis

To test the relationship existing between two variables a correlation analysis was done. A negative and positive correlation coefficient indicates a negative and positive correlation respectively. Table 4.11 shows the correlations

Table 4.11: Correlation Matrix

	ROA	M&A	Leverage	Liquidity	Management Efficiency	Firm Size
ROA	1					
M&A	0.773	1				
Leverage	0.463	0.316	1			
Liquidity	0.618	0.163	0.216	1		
Management Efficiency	0.652	0.161	0.233	0.462	1	
Firm Size	0.456	0.145	0.245	0.143	0.352	1

Source; Researcher (2021)

The study established the association between mergers and acquisition, leverage, liquidity, firm size and firm size and the financial performance of commercial banks using a Pearson Correlation analysis. The study findings presented in Table 4.6 established that there is a

significant positive relationship between financial performance and Mergers and acquisition (rho=0.773). Therefore, it can be implied that an increase in mergers and acquisition is associated with increased financial performance. Secondly, the findings showed that there is a positive significant relationship between financial performance and leverage (rho=0.463). This is an indication that an increase in leverage will definitely increase the financial performance of the commercial banks. Also, there was a significant positive relationship between liquidity and financial performance (rho=0.618) an indication that higher liquidity level increases the financial performance of the commercial banks. Further, there was a significant positive relationship between management efficiency and financial performance (rho=0.652) an indication that increase in management efficiency increases the financial performance of the commercial banks. Finally, the findings showed that there is a positive significant relationship between firm size and financial performance (rho=0.456) an indication that firm size have a positive impact on the financial performance of the commercial banks.

4.6 Discussion of Research Findings

The study revealed that return of assets of commercial banks increased significantly after mergers and acquisition. An implication that mergers and acquisition have a positive significant influence on financial performance of the commercial banks. In line with the study findings, CBK, (2017) indicated that M&A have enormously been of importance to performance of the commercial banks which have posted noteworthy financial performance contrasted with the banks which have not experienced M&A. The working collaboration is one of the points of M&A which thus influences the financial performance. It has been recommended that administrative financial production, research or advertising can be achieved by any business entities by guaranteeing sound financial management systems. Business entities can

likewise accomplish their targets by M&A which can have extreme objective of financial collaboration.

The study also revealed that leverage of commercial banks increased significantly after mergers and acquisition. An implication that as a result of mergers and acquisition leverage of the commercial banks increased which enhances their financial performance. In tandem with the findings of the study, Lucey (2015) opined that firms with high leverage are in great position to fiscally perform better. Extant researches dealt with the connection between leverage and performance of the firm and came to conclusion that high leverage diminishes the conflict amongst managers and shareholders leading to increase in performance and eventually a positive relationship develops.

The study also revealed that liquidity of commercial banks increased significantly after mergers and acquisition; an implication that as a consequence of mergers and acquisition liquidity of commercial banks increased thus improving the resultant banks' financial performance. Similar to the study findings, Wood, (1988) opines that Business entities with more liquid assets normally outperform the companies with less liquid assets because cash is readily available to cater for their needs at any point in time. The degree at which assets can be purchased or sold is the liquidity; this transaction not affecting the price of the assets in the market.

The study also revealed that management efficiency of commercial banks increased significantly after mergers and acquisition. An implication that as a result of mergers and acquisition management efficiency of the commercial banks increased thus enhancing their financial performance. In tandem with the findings of the study, Johnson (2005) is on the opinion that management efficiency is a situation where an organization utilizes its resources prudently in

order to maximize on its productivity level. Management efficiency is concerned with reducing resources waste with an aim of maximizing the firms' output level. In addition, management efficiency is aimed at increasing the efficiency of organization operations through sharing of duties whereby chief executive officer can as well act as a managing director.

The study also revealed that firm size of commercial banks increased significantly after mergers and acquisition. An implication that as a result of mergers and acquisition firm size of the commercial banks increased thus enhancing their financial performance. The results agree with Shim (2007) who concluded that the influence of firm size on financial performance of insurance companies improves significantly after merger and acquisition. Burca and Batrinca (2014) asserts that the size of the firm affects its financial performance negatively or positively. The advantage of big firms is that they can purchase gods at a reduced price unlike the small companies. This is due to the fact that the large organization can risk in diversifying themselves unlike the small company who do not take risks. These companies are able to respond to any change in the market due to their large sized-operations.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter provides summary of research findings from the study on how mergers and acquisitions influence the financial performance of commercial banks in Kenya. Further, it highlights policy recommendations in regard to M & A in commercial banks. The chapter also highlights the further areas for research.

5.2 Summary

The researcher was seeking to investigate the influence of M & A on the financial performance of commercial banks in Kenya. The population if the study in question included all the banks that had embraced mergers and acquisitions. The banks were 20 in total and the record was gathered from a period of 10 years as at 2008 up until 2018. Comparison to these banks was done during and after the M&A. this was checked statistically to signify the difference in value and t-taste was used as the paired sample.

The study established that the mergers and acquisitions resulted in an improvement in ROA for all banks except for Prime Capital Credit and Guaranty Trust Bank PLC. SBM Bank Kenya Ltd recorded the highest increase in ROA of 0.478 after the merger. Prime Bank ltd recorded the lowest ROA of 0.003. The companies' leverage ratios before and after merger and acquisition established that Guaranty Trust Bank, SBM Bank Kenya Ltd and Fidelity Bank Ltd had a significant improvement in the leverage after the merger and acquisition. Further a result shows that Kenya Commercial Bank Ld. recorded an insignificant improvement after the merger.

In addition, Jamii Bora bank recorded a much bigger increment on liquidity after adoption of merger. SBM Bank Kenya Ltd and Diamond Trust Bank Kenya Limited respectively followed on the increase respectively. This resulted to a conclusion that liquidity increased the results in commercial banks after mergers. In all the banks, there was a recorded increase in average management after and before the mergers and acquisition. Hence there was an increase in in total asset in Kenya Commercial Bank Ltd, Jamii Bora Bank ltd and Eco bank Kenya ltd. CFC Stanbic Bank ltd followed by showing a slight improvement of assets after M&A.

5.3 Conclusions

The study concludes that both mergers and acquisitions influence how commercial banks perform. They lead to the increase in return on assets hence an indication of commercial banks' financial performance improvement. The improvement could be attributed to acquisition and utilization of the new realized opportunities by the banks as a result of combined effect of human resources and financial resources so as to create synergies that brings about performance.

The improvement observed on the return on assets after M & A attests to the improved financial strength that commercial banks gain from the acquiring firm. The acquired banks also benefit from the pool of human resource translating to competitive advantage for the resultant firm. Moreover, M & A enable banks to gain from technological transfer from the acquiring firm resulting in better return on assets.

The study concludes that return on assets of commercial banks increased significantly after mergers and acquisition; an implication that mergers and acquisition have a positive significant effect on the financial performance of the commercial banks. The study also concludes that

leverage of commercial banks increased significantly after mergers and acquisition; an implication that as a result of mergers and acquisition leverage of the commercial banks increased thus enhancing their financial performance.

The study also concludes that liquidity of commercial banks increased significantly after mergers and acquisition; an implication that as a result of mergers and acquisition liquidity of the commercial banks increased which improves their financial performance. The study also concludes that management efficiency of commercial banks increased significantly after mergers and acquisition; an implication that as a result of mergers and acquisition management efficiency of the commercial banks increased thus enhancing financial performance. The study also concludes that firm size of commercial banks increased significantly after mergers and acquisition; an implication that as a result of mergers and acquisition firm size of the commercial banks increased thus enhancing financial performance.

5.4 Recommendations for policy

The recommendation therefore derived from this study is that the merger and acquisition process ought to be guided by clear strategies assented by each interest group. By doing this, resultant M & A will be free from governance issues that may affect the transition and subsequent profitability of the firm leading to adverse performance after merger or acquisition.

Additionally, commercial banks can also enhance their financial performance by undertaking mergers and acquisitions. The resultant banks benefit from financial, technology and human resource synergies leading to improved efficiency and risks diversification.

Acquisitions also enhance increased market share and dominance when a chief competitor is gained. This translates to increased profitability and hence firm value. In case a firm is unable to

grow organically because of limited resources, the firm may opt for external growth by consolidation of its activities with those of already well established firms via M & A which may aid in accelerating the speed of a firm's growth in a convenient and cheaper way.

In situations where a firm's resources are strained, the firm can consider getting into mergers and acquisitions in order to increase their total assets; as shown by the study results which showed that the average total assets increased for all the commercial banks post-merger. M&A enable commercial increase the asset base thus boosting their competiveness. In addition banks are also in a position to reduce liabilities by minimizing the debt equity ratio, and get capital at a lower cost as well as asset base growth as a result of acquisitions.

A recommendation is given that merged commercial banks ought to maintain leverage ratio at a standard level since too much debt is deemed unsafe as uncontrolled debt levels may cause credit downgrades whereas at the same time low debt-to equity ratios may also reveal that a company is not using the increased gains that financial leverage may bring.

5.5 Limitations of the Study

The 20 commercial banks that had experienced mergers and acquisitions during the study period made up the study's population. As a result, the findings can be applied to the twenty companies that made up the study population.

Secondary data was also utilised in the study, which came from the financial accounts of the institutions. Secondary data, on the other hand, is always historical in character and may not reflect the current state of the businesses.

The researcher also faced time constraint. Given that the study utilized secondary data which was obtained from several sources which included; Capital Markets Authority and the individual commercial banks. Despite the time constraints, the limited time available was adequately utilized for data collection and analysis.

5.6 Recommendations for Further Studies

A recommendation from this study is that additional in depth study be conducted to assess the major success factors for M&A of commercial banks. The findings will complement the findings of this research by revealing strategies that commercial banks can undertake to enhance their value through mergers and acquisition.

The study focused on merger and acquisitions and how they influence the financial performance of commercial banks in Kenya. This study recommends a study on mergers only and how they influence stock returns of listed firms in Kenya.

The study focused on merger and acquisitions and how they influence financial performance of commercial banks in Kenya. Merger and acquisitions however affect share prices volatility, firm liquidity and asset of the company. Merger and acquisition also affect employees and the company operations in general. The study therefore recommends a study on the effect merger and acquisitions on share prices volatility of firms and the other fundamental factors influenced by mergers and acquisitions.

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APPENDICES

APPENDIX 1: LIST OF COMMERCIAL BANKS MERGED OR ACQUIRED BETWEEN 2008 AND 2018

		Date of Merger/ Acquisition
	Mergers	
1.	Kenya Commercial Bank Ld. (Savings and Loan + KCB)	01.02.2010
2.	Prime Bank ltd (Prime Capital credit+ Prime Bank)	01.01.2008
3.	CFC Stanbic Bank ltd (CFC Bank + Stanbic Bank)	01.06.2008
4.	Jamii Bora Bank ltd (City Finance Bank+ Jamii Bora)	11.02.2010
5.	Spire Bank (Equitorial Commercial Bank + Southern Credit Banking Corporation)	01.06.2010
	Acquisitions	
6.	Eco bank Kenya ltd (EABS Bank Ltd acquired by Eco Bank Ltd)	16.06.2008
7.	Guaranty Trust Bank (Fina Bank acquired by Guaranty Trust Bank PLC)	08.11.2013
8.	Diamond Trust Bank Kenya Limited (Habib Bank Kenya Limited Acquired by DBT)	01.08.2017
9.	SBM Bank Kenya Ltd (Fidelity Bank Ltd acquired by SBM Bank Kenya Ltd)	10.05.2017

10.	I&M Bank Ltd (Giro Bank acquired by I&M Bank)	13.02.2017