A SURVEY OF FACTORS CONSIDERED IMPORTANT IN MERGER AND ACQUISITION DECISIONS BY SELECTED KENYAN BASED FIRMS

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Declaration

This project is my original work and has not been submitted for a degree in any other university.

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

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This research project is dedicated to

GOD THE FATHER,SON ,HOLY SPIRIT

AND MY EARTHLY FAMILY

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ABSTRACT

Mergers and Acquisitions seem to be a quick fix to business problems, involving the financial health of the firms. The problem is that these marriage's don't seem to last long, they are more polygamous than monogamous, the latter being the ideal.

This research project addresses the factors considered important by selected Kenya based firms, from different sectors, countries of origin as well as local ones, when they made Mergers and Acquisitions decisions.
These factors were then compared across sectors as well as by the different modes of origin i.e. local visa vis foreign.

The study looked at selected firms in seven important sectors of the Kenyan economy that had merged and acquired in the last 10 years. The research instrument used to collect data was a questionnaire with open ended and closed ended questions. Data was analysed using descriptive statistics and presented in tables and graphs for comparisons.

The critical factors considered when firms make merger and acquisition decisions were found to be the same regardless of business sector and modes of ownership (local or foreign). These factors from most important to least important were: a perfect fit, to improve business growth and revenues, to consolidate and be more competitive, globalisation, similarity in core competence, political factors, cost reduction, research and development, organisational culture and human factors.

Further research can be done to find out why cultural and human factors are least important in merger and acquisition decisions and what are the dangers this can cause to the well being of the new firm.

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AT & T	American telephone & telegraph
BP	British petroleum
EABL	East African breweries
GDP	Gross domestic product
GSK	Glaxo smithkline
IT	Information technology
ITT	International telephone & telegraphic corporation
KLM	Dutch airline
KPMG	Kenya Peat Mergwick
KQ	Kenya airways
MA	Mergers and Acquisitions
P &G	Proctar and Gamble
PWC	Price Waters Coopers
PLC	Public Listed Companies
R & D	Research and Development
SCM	Short Cycle Manufacturing
U.S.A	United States of America

CHAPTER ONE :INTRODUCTION

This study was done in seven sectors of the Kenyan economy considered important due to their size in terms of financial contribution to the Kenyan economy as seen in the 2002 economic review. Some firms from these sectors are also listed in the Nairobi stock exchange, and were also represented in the East Africa's most respected companies, a survey done by Nation media group and Price-Waterhouse-Coopers (Excellence deserves recognition 2001).The firms selected for these study have had mergers and acquisitions that have taken place within the last 10 yrs some have had more than one Merger and Acquisition in that period, specifically in Pharmaceutical and beer industry.

For along time , the U.S.A has set a pace for the global economy, though Europe and Asia may take on this role in this decade. According to Business Week (January, 2002),the world economy was estimated to grow by 1.1 % in the year 2002. Given the free flow of information around the world these days, applying the same values and standards everywhere is necessary for building sustainable relations.
As markets globalise, and the pace at which technology change continues to accelerate, more and more companies are finding mergers and acquisitions to be a compelling strategy for growth.

1.1 Examples of triggers that cause firms to Merge and Acquire

The forces of consolidation are shaping industry after industry according to Walter(March-April,1997)as narrated below:

Disappointing growth-: High rates of growth indicate an attractive market but when growth slows it brings loss of market share,

utilization of capacity is low, prize wars as companies try to gain market share through price competition.

The emergence of dominant product design tends to shift the basis of competition. Companies that standardise based on the product design attain production economies, making process innovation and integration more important. Rivals unable to make this transition or master the core technology will be forced to exit or be acquired (Mwaura, 2001) as happened between Castle breweries and East African breweries (EABL).

Scarce resource-: Lack of funds for R&D as with the pharmaceuticals, or access to funds for expansion in capacity or people skills building to acquire new technology and uncertainty about patent protection causes biotechnology companies to merge with Pharmaceuticals to provide adequate resources they need for new-drug pipelines.

Deregulation : In the U.S.A deregulation reduces artificial constraints on competition(Waters,2000). The U.S banking industry shrunk from 14,500 in number to 10,000 in 1995 in the wake of deregulation that permitted limited interstate banking, with more powerful national banks. Observers expect a further shrinkage to 5000 by year gone 2000 and beyond. The large banks would fuel this consolidations by investing heavily in technology and communications effectively, redefining economic scale in the industry. Small banks without resources to keep up would be candidates for take- over's in Mergers and Acquisitions.

Globalisation-:These broadens the scope of industry in which competition had been primarily domestic. As governments adopt common currency, standards and regulations, global sourcing and product development become much easier (Walter, 1997)

A technology discontinuity. A major change in an industry's technology makes previous processes and know-how obsolete as is

happened to EABL , glass making division when its customers for glass like GlaxoSmithkline and cocacola moved to plastic bottling. A similar scenario happened to the old East African industries, when their consumers preferred their cooking fat in Plastic containers as opposed to the tin technology that they had invested on, which became obsolete (Mwaura, 2001).

Emergence of innovative breakthrough technologies in an industry,(Walter,1997) Competency predators are innovators that have developed a new business model that offers the possibility of large economies of scale. Once they have mastered a competency in a given market with the help of IT, they apply the resulting skills and know-how to enter new regions, markets and industries. AT &T did this and successfully attacked the credit card business with a core competency of billing on a massive scale and a mastery of database marketing.

The above gleam picture has affected company growth and survival and most have had to think of Survival strategies like Mergers and Acquisitions to compete in emerging markets and to survive new entrants who have entered their sectors like the Kenyan beer industry which saw South African breweries come to fight them in their home market.(Market Intelligence,2001). Companies seem to be combining at a rate almost unprecedented in history and on a global scale. Mergers and Acquisitions are taking place across all business sectors (Vavora,1997),pushing these huge and pricey -cross border deals is the universal belief that industries will inevitably become more concentrated as the worlds markets become more globalised. Companies believe if they are going to be winners, they will have to sew-up economies of scale in manufacturing, branding and R& D which entails Mergers and Acquisitions .This is how companies hope to scare off potential competitors and dominate markets.

1.2 Factors considered important by firms when they engage in Merger & Acquisitions.

A combination of economic,political (antitrust laws),cultural differences ,social and competitive factors are important considerations in a new market place(Ansoff ,Mcdonell,1990) as shown below:

1.2.1 Distinctive technologies: which allow firms to stay on the leading edge and help attract and retain the most talented people. A firm should ask itself whether they have critical competence .For instance, according to Smith (Nov-Dec ,1997), Cocacola in 1980 had intimate knowledge of consumers, marketing and branding expertise, superior distribution capabilities but still could not succeed in the wine business because it did not have competencies imperative to wine business. It lacked the 10% ability to make quality wine, which is critical for success in the wine business.

Other issues faced are lack of relevant competencies (skills and technologies) as needed in the oil industry, mobile and telephony sector .In the beverage /drink industry, some firms were not thought of as rivals in the last century like the juice, milk and water producers ,they have become fierce contenders due to innovation and the opening of the market ,thus eating into the huge market that cocacola enjoyed in this sector.

1.2.2 Culture clash : All too many mergers undertaken with the highest of hopes have failed to deliver(Barret,1999). Too often culture conflicts and personality clashes hamper the new company's performance. Questions are being asked of the worlds biggest auditing firms like PriceWaterhouse coopers(PWC) formed in 1998.Pricewaterhouse

and Coopers were competitors for many years. Mergers born of defensive intentions are generally deemed unlikely to farewell because the two key management groups do not bled well together. Culture is an organizations vital sign when it comes to the success of the merger between any two firms , make it clear who is going to lead.

1.2.3 Shareholder value and cost of the deal. According to commerzbank research(1999),more than half of mergers ultimately fail to create shareholder value, due to merger costs exceeding expectations and conflict of interests between partners and interested parties. The value delivered by cutting costs has to be offset against the cost of the acquisition to assess how much money has been made. Merger fever was whipped up by the launch of the single currency the Euro in January 1 , 1999 as companies jockey for position in the continents new Euro zone(Business week, 1999)they are taking steps to attract investors by enhancing shareholder value through easy and low risk access of funds.

1.2.4 Ill conceived human resource integration strategy can see the firm loosing its most important component ,human resource hence human capital should be given attention during mergers.

1.2.5 Globalisation brought about liberalisation which lead to privatisation of public firms ,in kenya the business environment has experienced rapid changes and the firms survival has come under great threat due to a very competitive and rapidly changing environment(Mwaura,2001). With changes in legislations, firms are no longer protected by government policies to operate as monopolies or oligopolies. Local and multinational firms competing in this sectors have become extinct i.e Dawa pharmaceuticals which was a major player before the 80's ,others of a multinational orient have closed down

mainly in the pharmaceutical industry i.e Pfizer and Warner lambart and the banking sector as happened with ABN Amro bank.

1.2.6 High operating costs in infrastracture, logistics and communication as well as high interest rates have made costs of production high and the subsequent prices of goods and services to the consumer have become very high according to Mwaura(2001). Increasing costs of doing business have forced many to look for partners in similar industry to reduce such costs such R& D as with the pharmaceutical sector (Hakanson and labage ,1991),or in maintaining economical routes as with the Air industry.

1.2.7 Competition -: Heightened competition in Healthcare is creating big challenges for the industry, many companies fear it will threaten their capacity to undertake basic research. Threats from substitute products as with the generics in the pharmaceutical sector has brought a loss of market growth, low profits and declining growth in revenues. Those firms to succeed in the pharmaceutical sector will be those prepared to improve the marketing of drugs and they will also become better at the science of drugs (Kenneth ,1994).

According to Business week (2002), the lobbying power of cartels in the oil industry is no longer their strength and all the players are competing for a very small market due to a harsh economy.

1.2.8 Economic performance : According to poverty reduction strategy paper(2001-2004),there has been a declining economic performance in kenya from a high of 6.6% in 1960's to a low of negative 0.4% in 2002.As a result there has been declining levels of investment, productivity and competitiveness, distortions in markets and price structure. Increasing insecurity ,poor infrastructure has depressed the volume and efficiency of investment.

1.2.8 Un-employment due to a shrinking economy has reduced the consumer and industry purchasing power of goods and commodities(Business week 2002). The banking industry has experienced this threat through defaults on mortgages and foreclosure of accounts. A threat to tourism due to insecurity from terrorism and disease has affected significantly Air travel and Hotel accommodation, which relies on the same.

1.2.9 Anti-trusts laws: On the international scene(emerge,2000) we have regulatory bodies like the Federal trade commission(FTA) of U.S.A and European commission(EC) of Europe ,in Kenya we have the merger and monopolicies board and this can act as a force to contend with in any merger and acquisition.

1.2.10 Synergy can provide a big boost to the bottom line of most large companies. However synergy bias can also lead to overestimate of the benefits and underestimate of the costs involved. Synergy can become imperative rather than logical (Doz and Hamel, 1998). Not all sharing leads to competitive advantage, and companies can encounter deep organisational resistance to even beneficial sharing possibilities. These hard truths have led many companies to reject synergy prematurely yet it is very crucial when firms consider Mergers & Acquisations.

1.3 STATEMENT OF THE PROBLEM

According to Tom Davenport (Jan 1998), about half of all mergers enrich shareholders significantly while the other half produce depressing financial reports. It is not clear why this is so. Interrelationships among previously distinct businesses are perhaps the central concern of strategy. Companies that diversify outside their core business are often less successful because they take profits from good established business and put it into another business whose record of performance has been dismal. This usually happens due to the lack of the management talent to support the new products or the services that they were investing in. From the 1960's,through 2003, firms have been merging for reasons of growth and survival. The trend has been increasing. The conclusion that can be made from this is that Mergers and Acquisitions are strategies that have worked well over the years to help firms in all business sectors cope with a changing business environment. However, there is a big problem and a conflicting one according to studies on Mergers and Acquisitions. Favoro of Marakon Associates (Sep,2002),an international strategy consulting firm based in New york , says that years of research on Mergers and Acquisitions point to the same conclusion: Up to 75 % of them fail to create shareholder value. Recent studies done in the 90's by his firm on the most successful value creating companies found that many of them have been acquisitive and that in many markets across sectors ,.50% of these companies have grown primarily through acquisitions.

According to Dennis Carey (May-June,2000), diversification was the key reason for company failures in the 1960's,70's,and 80's. Examples of companies that failed due to diversification then were :

International telephone and Telegraphic corporation(ITT) and public limited companies in the U.S.A.

In contrast ,(Favora,2002)companies that are doing well today are very focused and are showing growth in share holder value as opposed to those which were more diversified in the 1960's to the 80's(Carey,2000) and failed to deliver share holder value . Given this poor picture that 50% of companies that are merging and have merged and acquired in the 90's have failed, it arouses an interest to want to find out what factors companies consider important when they make merger and acquisition decisions in Kenya for both local and international companies in an attempt to rationalise this big gap of failure and success rate in Mergers and Acquisitions. No studies have been done in Kenya on this issue.

1.4 OBJECTIVES

1. To determine the factors that are considered important by firms when considering Mergers and Acquisitions.
2. To establish if factors that are considered important by firms in mergers and acquisitions differ across sectors.
3. To establish if factors considered important by firms in merger and acquisition decisions differ between local and foreign firms.

1.5 IMPORTANCE OF THE STUDY

- The research findings and conclusions will help managers in decision making in Mergers and Acquisitions
- The study will contribute to the existing body of knowledge at the University of Nairobi , faculty of commerce on Mergers and Acquisition issues in Kenya in the different sectors of the Economy.
- The results of the study will act as secondary data for other researchers who may be interested in pursuing issues raised in the study

CHAPTER TWO :LITERATURE REVIEW

According to Prokesh (1997),the most important area for developing new concepts, methods and practises will be in the management of society's knowledge resources i.e Education., Mergers and Acquisitions
The growing trend is to merge based on core competencies, all in the name of becoming leaner and more focused. Companies are ridding themselves of subsidiaries that are draining their resources.

2.1 INDUSTRY BACKGROUND

This section provides an overview of Pharmaceutical, manufacturing, information technology, finance, air travel, oil and professional services industries.

2.1.1 Pharmaceutical Industry. According to Huellmantel and Vaghefi(1999),the U.S.A pharmaceutical industry remains the leader in the world Pharmaceutical business. Competitiveness and innovative changes are frequent, largely due to demands for medical cost containment, mergers and Acquisitions. The U.S.A pharmaceutical industry historically one of the nation's most profitable and fastest growing segments of the economy, is faced with an increasingly difficult operating environment in the years ahead and so is the local Kenyan situation .The following changes have been observed-:

Mounting competitive pressure from similar product lines or generics that are cheaper. Generic drugs offer the toughest competition that has led to some of the Mergers and Acquisitions that have been recorded in the last few years.

Changes in customer profiles and purchasing power: Consumers are moving to herbal preparations as opposed to conventional drugs.

A challenge due to high drug costs. Managed health care by insurance, health management organisations ,Governments and corporations have responded to these cost and their sources by establishing medical schemes.

Mergers-: The pharmaceutical industry is the fastest growing sector in Mergers and Acquisitions worldwide, the Glaxo-Smithkline merger comprises of the Glaxo-wellcome merger, Smithkline-nephew-beecham -sterlinghealth merger . Submergers within the Mega are on the increase. New strategy development entails discovery and development of new types of products and finding ways to increase sales of existing products ,profitably can only be realized through Mergers and Acquisitions Vaghefi(1999).

New regulations by regulatory bodies and anti-trust laws in Europe, U.S.A and local country bodies which are becoming stiffer.

The increasing over the counter products, are putting a lot of competitive pressure on the prescription products. This has lead to a situation in which the prescription drugs are being sold over the counter at reduced prices, stagnation and, in some cases decline in profit margins.

Competitive advantage in this sector rests on innovation, which acts as a barrier to entry into the industry.

2.1.2 Manufacturing (food, beer and beverage sector)-: The initial capital required to build the facility and purchase the necessary equipment is obviously high(Vaghefi and Huellmantel,1999). Advertising and marketing for a new brand is also very high and that is why most new competition comes in the way of mergers between already established firms. For, instance, Kenya Breweries acquired already built plants like Kibo in Tanzania and Uganda breweries in Uganda(Mwaura ,2001).

2.1.3 Information technology-: Deregulation in this sector has brought competition and high market growth rates which have resulted from high demand for internet, cell-phone and related electronic services(Business week ,2002).Fear of cyber terrorism and computer virus are likely to increase growth in this sector due to purchase of security software ;data storage software firms are likely to gain from purchases of disaster -recovery systems; high revenues are likely to accrue from increased sell of chips for mobile handsets and internet -capable hand-helds such as compaq computers ipaq. However, this sector is characterised by high operating costs due to heavy advertising and cut throat pricing to gain market share. There are more Mergers and Acquisitions in cable and TV in the U.S as midsize players come together to address the growing demand for digital services and to achieve greater scale as shown by the merger between Comcast corps and AT & T cable systems.

2.1.4 Finance sector -: The banking industry is far better prepared for a downturn in the world economies than it was in the early 1990's.Banks are more geographically diversified and have had stricter capital standards which do help to keep them in check. Banks are also getting better at hedging their corporate loan portfolios too. In Kenya, Standard chartered Bank, Barclays bank, City group and ABN Amro were ranked in that order from most to least profitable banks in a category of 31 banks in Kenya. They took the first four positions according to Mwaura (April/May, 2001). Most shareholders of private institutions in Kenya, instead of recognizing the potential commercial benefits to be derived from mergers, are more concerned in what will be their role in the merged bank. They want to know if they will remain chair-man or whether they will exercise the overbearing influence in the new set-up in management. Unfortunately, these concerns tend to be

non-commercial drivers that often lead to the banks collapse or demise. ABN Amro has since ceased operation in Kenya due to fierce competition

2.1.5 Air travel industry-: when the hotel industry suffers, Airlines suffer because 64% of journeys involving a hotel stay include an Airline trip(Business week , 2002) .In the wake of world terrorism and a world economy in recession, analysts in PricewatersCoopers think weak Air carriers will be forced to merge with one another for survival.

2.1.6 Oil industry-: In 2002,the oil industry, thrived in record profits due to high energy prices and efficiencies eked from Mergers and their related synergies as happened in Europe with the BP and Exxon-Mobil corporations Merger and Acquisition .According to Alfred Chandler(1999), high -technology industries are defined by what he calls paths of learning .In market economies, the competitive strengths of industrial firms rest on learned organisational capabilities which may be achieved through Mergers &Acquisition 's. The CEO of the Chevron Texaco merger(2001) said " when you blend the best talent and the latest technology into one world-class company, you do more than expand operations, you broaden horizons, grow opportunities and create promise.

2.1.7 Professional services-: These include consultancy, accounting /audit and education(Business week,2002). They form the category of services that are out- sourced hence they do not necessarily have to be part of a firm's structure. Out-sourcing will remain strong as companies seek to boost operating efficiency. Demand for consulting, however will decline as companies seek to cut operational costs. For consultancy to hence thrive, it must show it can make a contribution to the bottom line of a firm.

2.2 The benefits of Synergy

According to Goold and Campbell (1998),the word synergy is derived from the greek words synergos which means " working together" In business usage ,synergy refers to the ability of two or more units or companies to generate greater value working together than they could working apart . Most business synergies take one of the following six forms:

Shared know -how: Units often benefit from sharing knowledge or skills. They may for example, improve their results by pooling their insights into a particular process, function or geographic area. The know-how they share may be written in manuals or in policy and procedure statements but very often it exists tacitly, without formal documentation. Value can be created, by exposing one set of people to another who have a different way of getting things done. The emphasis that many companies place on leveraging core competencies and sharing best practises reflects the importance attributed to shared know-how.

Shared tangible resources : Units can sometimes save a lot of money by sharing physical assets or resources. By using a common manufacturing facility or research laboratory, for example they may gain economies of scale and avoid duplicated effort. Companies often justify acquisitions of related business by pointing to the synergies to be gained from sharing, for example, Daimler Chysler uses the component sharing strategy whereby the Sedan car uses a rear wheel driving transmission of the Mercedes car model.

Pooled Negotiating Power : By combining their purchases, different units can gain greater leverage over suppliers reducing the cost or even improving the leverage over suppliers, reducing the cost or even improving the quality of the goods they buy. Companies can also gain similar benefits by negotiating jointly with other stakeholders such as

customers , government or universities. The gains from pooled negotiating power can be dramatic.

Co-ordinated strategies: It sometimes works to a company's advantage to align the strategies of two or more of its business. Dividing up markets among units may for- instance, reduce inter-unit competition. Co-ordinating responses to shared competitors may be a powerful and effective way to counter competitive threats. Although co-ordinated strategies can in principle be an important source of synergy, they're tough to achieve. Striking the right balance between corporate intervention and business-unit autonomy is not easy.

Vertical integration : Co-ordinating the flow of products or services from one unit to another can reduce inventory costs, speed product development, increase capacity utilisation and improve market access. In process industries such as, Pharmaceuticals and forest products, well -managed vertical integration can yield particularly large benefits.

Combined Business creation: The creation of new businesses can be facilitated by combining know-how from different units, by extracting discrete activities from various units and combining them in a new unit or by establishing internal joint ventures or alliances. As a result of the business world's increased concern for corporate regeneration and growth, several companies have placed added emphasis on this type of synergy. For example, in the pharmaceutical industry, sales representatives selling consumer products can also be trained to promote pharmacy over the counter products hence shared between the two units of consumer and pharma in the pharmaceutical industry. Even synergy that is clearly defined often fails to materialise because, instead of cooperating, business units often compete.

2.3 Limitations of synergy

According to Goold and Campell(1998),corporate executives have strong biases in favor of synergy which can lead them into ill-advised attempts to force business units to cooperate even when the ultimate benefits are unclear. But executives can separate the real opportunities from mirages according to Porter(1998). They simply need to take a more disciplined approach to synergy.

2.4 Types of synergy bias

Synergy bias leads executives to overestimate the benefits and under-estimate the costs of synergy. If the total cost of doing a particular process for the merged company is greater than the sum total of the two separate businesses then it is not worth the effort of having it under one roof. For example outsourcing distribution of bulky products vis via running own flight. Following are types of synergy biases that are likely to occur according to Goold and Campbell(1998) :

Parenting bias-: A belief that synergy will be captured only by cajoling or compelling business units to cooperate. The parenting bias is usually accompanied by the skill's bias.

Skills bias-: The assumption that whatever know-how that is required to achieve synergy will be available within the organization. Lack of the right skills can fatally undermine, the implementation of any synergy initiative, what's more, learning new skills is not easy especially for senior managers with ingrained ways of doing things.

Upside bias-: Synergy has its positives and negatives collectively known as "knock on effects" which are-:

It can help or harm an effort to instill employees with greater personal accountability for business performance.

It may reinforce or impede an organisational change.

It may increase or decrease employee motivation and innovation. It may alter the way unit managers think about their businesses and their roles for better or for worse.
In evaluating the potential for synergy, corporate executives tend to focus too much on positive knock-on effects while overlooking the downsides, known as upside bias according to Goold and Campbell(1998).

The above biases make synergy seem more attractive and more easily achievable than it truly is. Clarifying the real objective and benefits of a potential synergy initiative that is " sizing the prize" is the most important discipline in making sound decisions on synergy.

2.5 CONCEPTUAL MODELS

Two conceptual models are relevant to this study, namely the value chain Model (Porter 1998) and Alliance purpose model (Doz and Hamel ,1998).These models are reviewed below:

2.5.1 Importance of synergy in mergers and acquisitions

According to (Porter, 1998) ,imagined synergy is much more common than real synergy. Ansoff (1990) calls it perception vis-a -vis reality .This fact was demonstrated when General Motors purchased Hughes aircraft simply because cars were going electronic and Hughes was an electronics concern. This example amply demonstrates the folly of paper synergy. But the need to capture the benefits of relationships between businesses has never been more important than now. For instance, if we borrow from the concept of the value chain, every business unit is collection of discrete activities ranging from sales

to accounting that allow it to compete. These are referred to as value activities, which, according to Porter(1998))are :

a)**Primary activities** -:Which create the product or service ,deliver and market it, and provide after-sale support. They include inbound logistics, operations, outbound logistics, marketing and sales and service.

b) **Support activities**-: These provide the inputs and infrastructure that allow the primary activities to take place. They are company infrastructure, human resource management, technology development and procurement.

The activities explained above indicate the value chain that defines the two types of inter-relationships that may create synergy namely-; Company's ability to transfer skills or expertise among similar value chains

The ability to share activities for example two business units can share the same sales-force or logistics network .

Similarities allow sharing of knowledge and they also create opportunities which lead to a competitive advantage of the merged firm according to Porter(1998). Transferring skills can lead to synergy if the similarities among businesses meet three conditions, namely :

The activities involved in the business are similar enough that sharing expertise is meaningful. Broad similarities(like marketing intensiveness) or common core process technology like drilling or packaging) are not a sufficient basis of merging because the resulting ability to transfer skills is likely to have little impact on competitive advantage of the merged firm.

The skills transferred represent a significant source of competitive advantage to the new merged firm.

The skills transferred represent a significant source of competitive advantage to the new merged firm and that the expertise or skills transferred are both advanced and proprietary enough to be beyond the capabilities of competitors. The transfer of skills should have a positive impact on shareholder value.

Sharing of activities among Kenyan firms has been observed. For example Proctor and Gamble(P&G) for example employs a common physical distribution system and sales force. Tibett and Bretton ,a leading distribution company will handle such diverse lines as pharmaceuticals, liquor, consumer products(cooking fat, detergents)through super-warehouses(Market intelligence 2001).

The ability to share activities is a potent basis for synergy because sharing often enhances synergy by lowering costs or raising differentiation. Sharing can lower costs, it can achieve economies of scale, and can boosts the efficiency of a firm in the utilization of its assets or it may even help a firm move more rapidly down its learning curve. The costs of General Electrics advertising division are low because they are spread over a wide range of appliance products according Welch (1998).

Sharing can enhance the potential for differentiation as well as reduce the cost of differentiation e.g A shared order processing system may allow new features and services that a buyer will value. A shared service network may make more advanced , remote servicing technology economically feasible. Sharing will allow an activity to be wholly configured in ways that can dramatically raise synergy and hence bring about competitive advantage (Porter,1998).

2.5.2 Importance of Strategic Alliance

According to (Doz and Hamel,1998) in their book on alliance advantages , three major purposes of alliances(Mergers and Acquisitions) are:

Co-option which turns potential competitors into allies and providers of complementary goods and services, and this allow new businesses to develop. Firms with complementary goods contribute by creating networks and economies of scale in favour of the coalition(M &A). Potential rivals who were a threat are effectively neutralised by bringing them to the alliance. British Petroleum(BP) is the most profitable of the major oil companies. In Europe, BP has merged its European fuel and lubricant business with Mobils .This landmark deal struck in 1996 offered an opportunity to create a first-tier player in an oversupplied mature market. The chief executive in (Prokesh, 1997) said that"learning is at the heart of a companies ability to adapt to a rapidly changing environment. It is the key to being able to identify opportunities rapidly and fully. This was the case with this type of alliance between BP and Mobil Europe". BP used co-option to contribute to value creation and to erode the competitive strength of the dominant industry players in Europe(HBR 1997)

Co-specialization is a synergistic value creation that results from the combining of previously separate resources positions, skills and knowledge sources. Partners contribute unique and differentiated resources, skills, brands, relationships, and tangible assets which create value when they are co-specialised. They become more valuable when bundled together in a joint effort than when kept separate.

Learning and internalisation are core competencies, which are not for sale on an open market, when they can be learned from a partner and

internalised and exploited beyond the boundaries of the alliance itself. They become all the more valuable and thus leveraged broadly into other activities and businesses beyond those covered by the alliance.

Being global is the most essential characteristic for future success as characterised by the websites of global companies with slogans like "coke is refreshing the world" and P &G 's " cleaning it".

BP in Europe uses distinctive assets, technologies like giant oil and gas fields to produce outstanding returns and achieve sustainable growth according to Browne(1997) . These are low cost and few of them, their refining and marketing groups offer large market shares, stations with high volumes and refineries that perform in the top quartile of their markets are distinctive. As Michael porters says in his book on Competition(pgs 112, 1998) ," the challenge of developing or reestablishing a clear strategy is primarily an organizational one and depends on leadership." Strong leaders like John Browne head of BP's Exploration and production(BPX), who are willing to make choices are essential.

2.5.3 Trends in Mergers and Acquisitions Across Sectors

Statistics show that almost 80%of M&A 's involving companies that seem to have a synergistic financial and strategic fit can fail if there is a lack of cultural alignment according to the commerzbank research (1999). Chevron Texaco recognised that risk and learned from it from their competitors who had recently merged and had had culture clash.(Chevron Texaco newsletter,2000)

Daimler-chrysler (Bower,2001)started as a merger of equals in an industry the two companies analysis revealed to have staggering over-capacity . The top management of both companies recognised the particular assets and qualities that made the other a perfect fit. But startling differences in their management approaches soon disrupted their working relationships. The perfect fit that seemed so obvious in the abstract was foundering on very real fundamental differences in the way two groups of managers thought about themselves, their roles and their companies.

Geographic roll-up ,which include access to capital, national marketing, modern technology, competitive threats and geographic entry has had its influence too on Mergers &Acquisitions(Bower,2001). Accounting firms in the U.S.A were assembled this way whereby, resources were not an issue, hence the challenge for this kind of deals is to introduce the company to new processes and values. When Quaker oats acquired Snapple for instance, it found that its advertising and distribution process were wholly unsuited to the target company's product line. Mark and Spencer found that its famed distribution systems couldn't cope with Canadian geography when it acquired Peoples department store.

Britains Imperial chemical industry (ICI) and U.S Zeneca according to Marcus(1995) merged and later de-merged due to mismatch between its role as corporate parent and the needs of its businesses. Acquisitions may actually increase a company's vulnerability to competitive attack because the demands of integration can divert attention away from competitors.

They also create an opportunity for competitors to poach talent, while organizational uncertainty is high says Sirower (1999). For example,

After Duets bank had acquired Bankers trust in Europe and was forced to pay huge sums of money to retain top performing people in both organizations.

Mergers and Acquisitions are a critical strategic tool for growth in the new economy(Chaudhuri & Tabrizi, 1999). The need for speed forces companies to acquire rather than build. The Smart internet and communication companies are using their high market position and currency to acquire companies quickly, solidify their positions as the new economy takes shape. For example World-com is one of the top two telecom companies in the world created this way. Each company needs to carve out its space for no company knows where its going to end up and merger and acquisition may be the only way. In 1998 Mergers and Acquisitions in U.S were 12,356 for a total value of $ 1.63 trillion compared with 4066 deals worth $ 378.9 billion in 1980(Nov-Dec ,1999). Mergers and Acquisitions remain the quickest route companies have to new markets and to new capabilities.

Know what your buying the further one gets from their home base the harder it is to be confident of that knowledge.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 POPULATION

The population of interest in this study comprised of selected firms that had merged or had been involved in acquisitions in Kenya in the last 10 years, whether of local orient, foreign orient or both. For the purpose of the study selected firms from different sectors were studied. The list of these firms is presented in the table 2: below

Table 1: Firms that have been involved in merger/Acquisitions in Kenya the last 10 years and their respective sectors.

SECTORS	FIRMS REPRESENTED
PHARMACEUTICAL	GSK,AVERTISPASTEUR,ASTRAZENECA ,NORVATIS,PFIZERWANALAMBART
INFORMATION- MOBILE AND PC,INTERNET	SAFARICOM,KENCELL,AFRICANONLINE,COM PAQ/HP
MANUFACTURING- FOOD AND BEVERAGE	EABL,,COCACOLA AFRICA DIVISION,THE UNGA GROUP
PROFFESIONAL SERVICES - ACCOUNTANCY/EDUCATION/CONSULTANCY	PRICEWATERSCOOPERS, KPMG, ALEXANDER FORBES,EARNEST YOUNG
FINANCIAL	CITYGROUP,STANDARD GIRINDLAYS,NIC BANK
AIR TRAVEL	KQ/KLM,
OIL INDUSTRY	SHELL/BP,TOTAL,CHEVRON TEXACO,KENOL/KOBIL

Sources: CBK merger information publication,2000,KPMG merger department

3.2 DATA COLLECTION

The study used both primary and secondary data (Company newsletter). The secondary data was in the form of a company merger newsletter, If and when available it was used as a data verification tool.

The primary data collection instrument was a structured questionnaire comprising of both open and close-ended questions. The questionnaires were self-administered, oral interviews were also conducted after questionnaires had been returned to elicit more information that was not clear from the questionnaire. The questionnaire were in two sections-:

Section 1: Sought after general information while section 2 , collected information specific to objective one.

A guide was also prepared for use by the research for the comparative analysis of objective two .It is attached as appendix two.

3.3 DATA ANALYSIS

The following quantitative and qualitative techniques (Jones 1988) were used in the analysis:

1) Descriptive statistics such as summarized tabulations of frequencies, mean, standard deviations, percentages, and rankings were used to outline and describe the variables under investigation.
2) Factor analysis was used to identify the factors considered important in merger and acquisition decisions.

CHAPTER FOUR: DATA ANALYSIS AND FINDINGS

Out of 24 firms that were sampled, 19 responded. This was 80% response rate. 20% of the firms declined due to issues of confidentiality (two of the firms were foreign owned while three were locally owned).

The data analyzed and presented in this chapter was obtained from: changes in the industry, reasons for merging and acquisition, what made the firms unique in their sectors, their sources of learning and identified synergies accrued from the mergers and acquisitions .

This was to address the first objective, which was concerned with factors considered important in making merger and acquisition decisions. Amongst other things,the data was classified by ownership (foreign visa via local).

Table 2: Distribution of firms by country of Origin

COUNTRY	FREQUENCY	PERCENT
South Africa	1	5.3
USA	6	31.6
UK	2	10.5
France	2	10.5
British and Dutch	1	5.3
Switzerland	1	5.3
Kenya	6	31.6
Total	19	100

As shown in table 2 , majority of the firms surveyed were from Kenya and the U.S.A (31.6% each).This was followed by U.K and France(10.5% each).

Table 3: Factors considered important by firms in merger and acquisition decisions

FACTOR	FREQUENCY	PERCENT
Perfect fit(Synergy)	16	15.5
Geographic presence(globalisation)	12	11.7
Organisational culture	5	4.9
Similar core competence	12	11.7
Synergies in R&D	6	5.8
To consolidate and be more competitive	16	15.5
To improve growth and revenues	16	15.5
Political factors i.e antitrust laws	8	7.8
Human factors	5	4.9
Cost reduction	7	6.8
TOTAL	**103**	**100.0**

As shown table 3, the cardinal factors considered by firms when they make merger decisions from top priority to least were: a perfect fit(15.5%), to improve growth and revenues(15.5%), to consolidate and be more competitive(15.5%), globalisation(11.7%), Similar core competence(11.7%), political factors(7.8%), cost reduction(6.8%), Synergies in Research and development(5.8%) and lastly human and cultural factors(4.9% each).

The issue of focus and synergy as opposed to diversification was demonstrated, indicating that firms are asking themselves what they are good at and looking for others with similar goals and visions.

The human consideration has diminished in importance compared to technology; this poses a big danger because organisations achieve their goals through people, making the human component very key as opposed to what this study showed.

Figure 1 on page 37, presents sectoral distribution of factors considered important in merger and acquisition decisions.
Across the sectors a similar trend holds with the top three priorities of a perfect fit, to consolidate and be competitive and to improve growth being ranked highly by the sectors. However the first and second were unanimously ranked by all respondent firms, showing that survival for the firm is very crucial as well as the issue of focus and similarity of the business. This shows that firms want to do what they are good at and thus merge and acquire firms that are in a similar business.

Cultural and human aspects were given minimal consideration, with the banks not considering them at all ,apparently due to their dependency on computers.
Research and development was critical for the pharmaceutical and Air sector only. This is surprising , given that innovation is a cutting edge strategy for the 21st century(Doz and Hamel,1998) for all sectors. Moreover dominant changes taking place in the sectors (table 4,pg 38) showed that, emergence of new product designs, globalisation and emergence of innovative breakthrough technology as great threats. Therefore, to counter such threats we would expect research and development to be amongst the top priority in all sectors not just pharmaceutical and Air sectors.

Figure 1: Sectoral distribution of factors considered important in merger and acquisition decisions

Y axis: FACTORS INFLUENCING MERGER AND ACQUISITION DECISIONS

X axis: RATING OF IMPORTANCE OF FACTORS

KEY: RIGHT SIDE OF FIGURE, ARE THE SECTORS

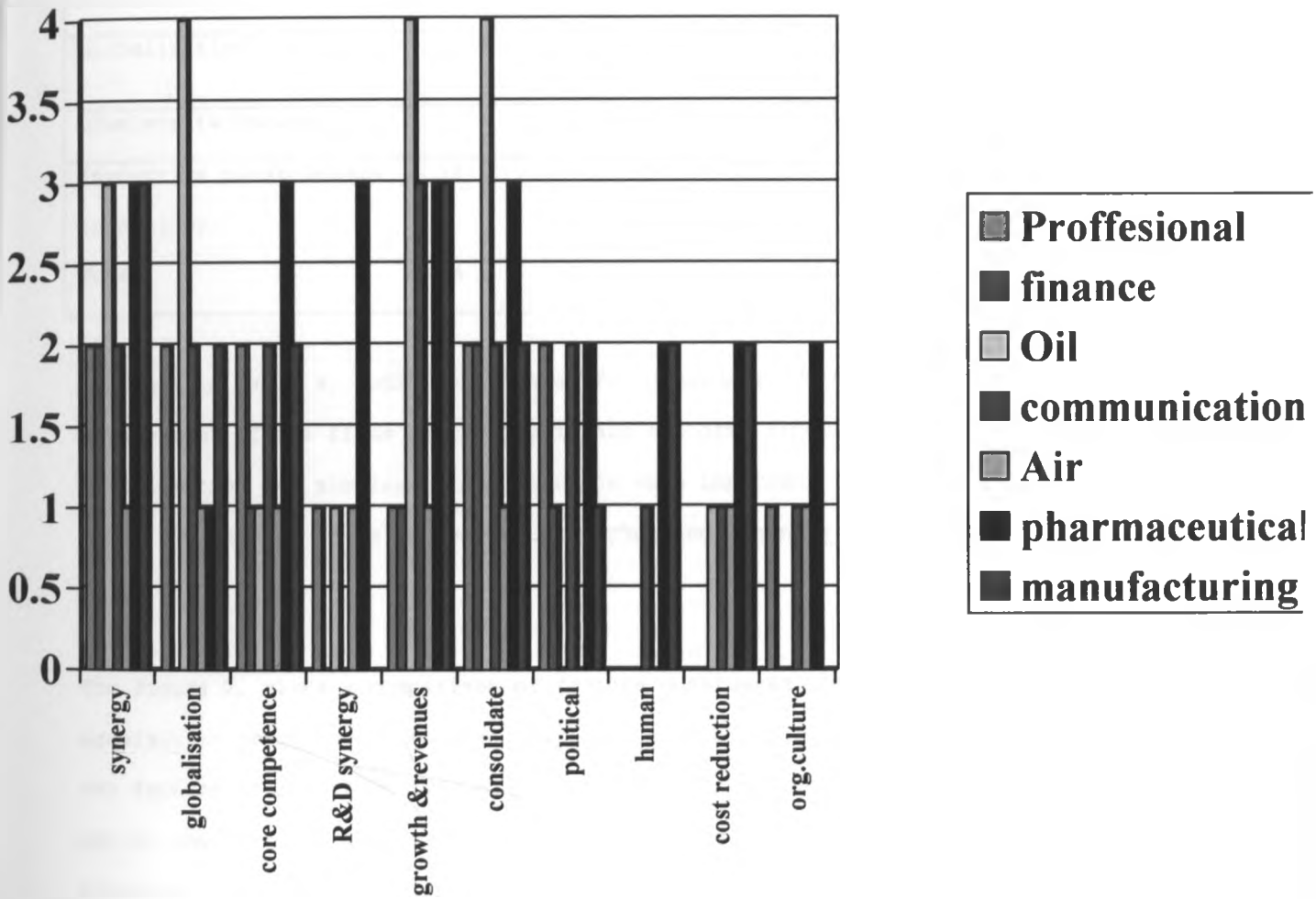


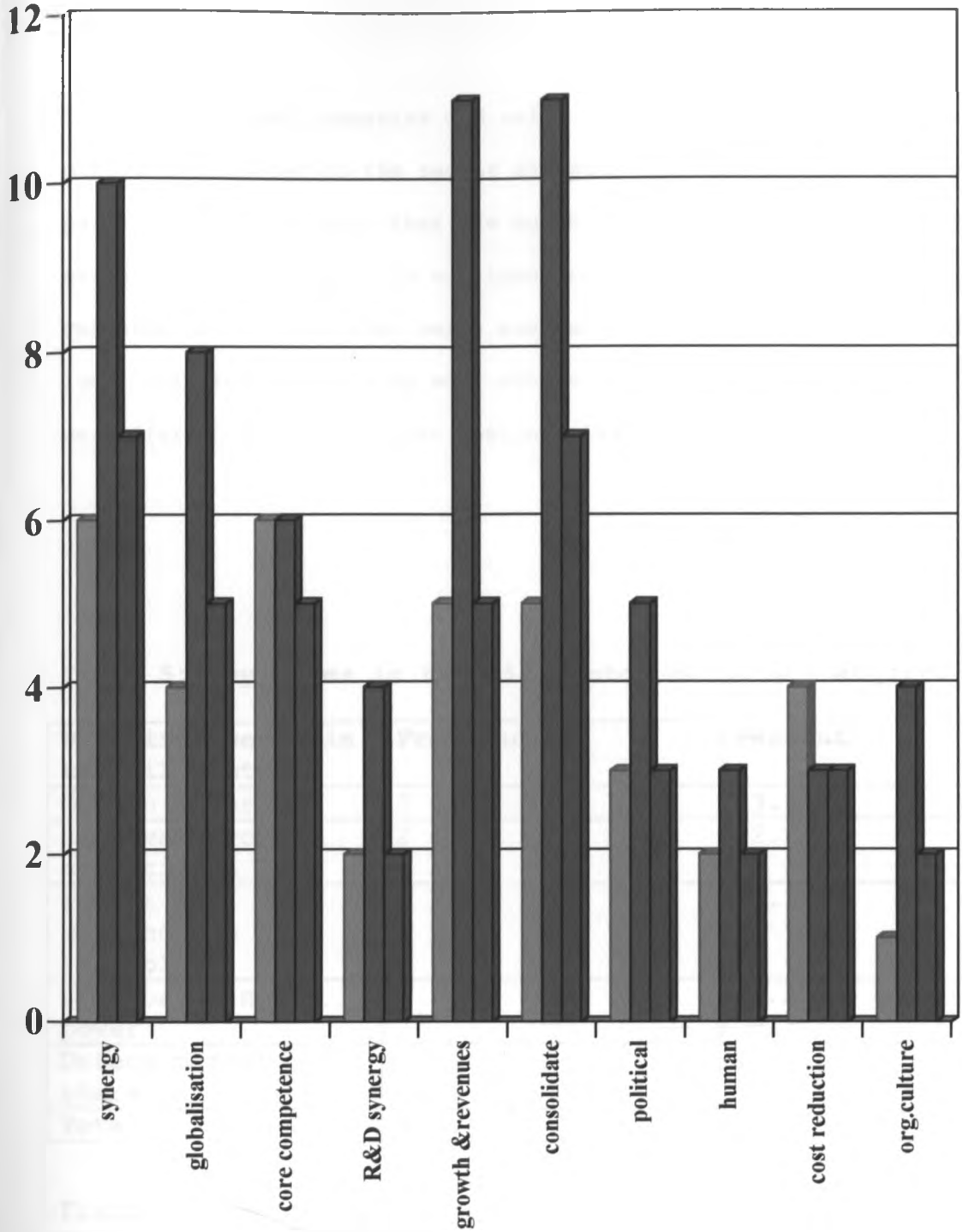
Table 4:Changes taking place in the environment of the firms sector of operation

CHANGES IN THE ENVIRONMENT	FREQUENCY	PERCENT
Declining growth	6	9.4
Stagnant growth	6	9.4
Emergence of new product designs	14	21.9
Deregulations	7	10.9
Globalisation	13	20.3
Obsolete technology	4	6.3
Innovative breakthrough technology	14	21.9
TOTAL	**64**	**100**

Findings in table 4, indicate the need for consideration of research and development of the firms technology in all sectors. Findings also explain why globalization and similar core competence were important factors when firms merge and acquire so as to respond to a changing business environment.

The figure 2, gives a comparison of factors considered important in merger and acquisition decisions by foreign and local companies across sectors. Once more, the factors of a perfect fit, to improve growth and revenues, to consolidate and be competitive, similar core competence and globalisation are top priorities.

Cost reduction was a critical factor to companies locally owned and not so much for the foreign owned. This can be attributed to the high cost of doing business in Kenya, though the foreign owned firms may not feel the high impact due to corporate parent support.



X axis: Factors influencing merger and acquisition decisitions

Y axis: Rating of importance OF Factors

Key: Right hand side;ownership(local,foreign) and sector

Figure 2: Distribution of factors that influence mergers and acquisitions by ownership(local,foreign) and sector

The foreign owned companies did value the human and cultural issues more when compared to the sector averages than their local counter parts. This could imply that the human integration strategy in mergers and acquisition locally is not imperative. Largely due an existing resource pool of the same being available readily, and synergies in the local cultures as pertains work ethics and management styles which may be different for an American setting visa vis a European one.

Table 5: Why firms in the oil sector merge and acquire

Why firms merge in the oil sector	**Frequency**	**Percent**
Growth in profit	3	33.3
Survival from competition	2	22.2
To get a distinctive technology	1	11.1
Gain bargaining power	2	22.2
Defend market share	1	11.1
Total	**9**	**100**

Firms in the oil sector merge and acquire due to a need for growth and profits (33.3%), survive from competition and gain bargaining power (22.2% each), to get a distinctive technology and defend market share (11.1% each). This implies mergers and acquisition are an important strategy to combat threat of new entry in this sector more than merely a strategy for global presence.

CHAPTER FIVE:SUMMARY,CONCLUSIONS AND RECOMMENDATIONS

5.1 SUMMARY

According to (Chaudhuri & Tabrizi,1999),more companies are finding mergers and acquisitions to be a compelling strategy for growth. The study showed that when firms merge and acquire, they consider these factors as important ranked by highest to lowest considerations: **A perfect fit, to improve growth and revenues, to consolidate and be more competitive, geographic presence, similar core competence, political factors, cost reduction ,organisational culture, cost reduction and lastly human factors .**

The study has proven that synergy, the issue of similarities and sharing, and the concept of a perfect fit that is firms acquiring and merging with others in similar business, similar goals and vision, are key factors considered important. This can then explain tremendous growth of the firm's revenues achieved regardless of sector or nature of orientation . Firms merge and acquire to achieve growth in their revenues and for the very reason consolidate operations to be more competitive in their sector of operation ,implying greater value was achieved by working together than they could working apart.
Important to note was the poor rating given to culture given that it is a fundamental ingredient for the success of mergers and acquisition(Barret,1999)

There were aspects of sharing due to similarities and this created opportunities. This finding is consistent with Porters model of the value chain(1998)which defines the two types of interrelationships that interact to create synergy.

5.2 CONCLUSIONS

Strategic mergers designed to add capabilities(core competences, synergies ,revenues and growths to create new business(consolidate and become competitive) have a 87% chance of success(Booz ,2001).

The results of this study disagree with those of Isaboke(2001) in the oil sector where he found that mergers and acquisition were least important in responding to threat of new entry into the industry. This study found that firms in the oil sector merge and acquire to improve revenues, survive from competition and defend market share more than they do to globalise as Isaboke(2001) implied.

The study agreed with Alfred chandler(2000) , Koigi(2002) and Wamathu(1999) as far the use of technology expertise is concerned as a competitive strength acquired through mergers and acquisitions.
90% of these mergers and acquisitions studied were acquisitive and hence will most likely succeed according to Booz(2001) , Favora(2002) and Germini,Young(2002).

Cultural factor is given least consideration as was also found by Muriuki(2001).This is a major concern in this study in that culture in many studies has proved to be what makes a merger or acquisition, succeed or fail. Daimler-chrysler failed due to overlooking culture that was different between Europeans and Americans, Bower(2001) and Barret(1999). According to the learning of the Chevron Texaco merger, C-sphere(2001),Almost 80% of mergers involving companies that seem to have a synergistic strategic and finacial fit as was the case for all

firms studied, fail because of cultural alignment which is a key success factor for a merger and acquisition.

5.3 RECCOMENDATIONS

When firms merge and acquire the factor of culture and human resource should be imperatively considered. Could it be why nine out of the 24 studied still intend to merge in the future?

To stay at the top firms need to give more attention to research and development which births innovation to avoid their distinctive technology becoming obsolete or irrelevant.

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APPENDIX ONE

SECTION 1:

1. List companies with which you have merged/Acquired in the last 10 years?

_____

_____

2. What are the changes taking place in your industry?
(*May tick all as applicable*)

Declining growth	☐
Stagnant growth	☐
Emergence of new product designs	☐
Deregulations	☐
Globalisation	☐
Obsolete technology	☐
Emergence of innovative breakthrough technology	☐

3. Who are your closest competitors in your industry?

_____

4. What business are you in? (*Please tick as appropriate*)

a)	Pharmaceutical	☐
b)	Beer	☐
c)	Beverages	☐
d)	Banking	☐
e)	Consultancy/Audit/Accounts	☐
f)	Oil	☐
g)	Communications	☐
h)	Other, *Please specify*:	☐

_____

5. Where would you rate your business turnover per annum?

a)	Ksh. 500 Million and below	☐
b)	Ksh.501 Million - 1.0 Billion	☐
c)	Ksh. 1.1 Billion - 1.5 Billion	☐
d)	Ksh 1.6 Billion - 5 .0Billion	☐
e)	Ksh 5.1 Billion - 10.0 Billion	☐
f)	Ksh 10.1 Billion - 20.0 Billion	☐
g)	Ksh Over 20 Billion	☐

6(a) Is your company a local one?

Yes ☐ No ☐

6(b) If No, Specify country or countries of origin?

_____

7.Why did you merge with & acquire the other company?

a) Need for growth in profits ☐
b) Need for survival from competition ☐
c) Need to get a distinctive technology ☐
*(If you tick **(c)**, Please specify)*

_____

d) Need to utilise capacity ☐
e) Need to gain more bargaining power ☐
f) Need to defend market share ☐
g) Need to reduce production and marketing costs ☐
h) Need for more product lines ☐

8.What are the sources of learning in your organization?
(May tick all as applicable)

a) Own experience ☐
b) Contractors ☐
c) Suppliers ☐
d) Partners ☐
e) Customers ☐
f) Companies outside our business ☐
g) Breakthrough thinking ☐

9(a). What is your purpose/vision.?

_____

9(b). How does your purpose/vision compare to that of the separate firms of your Merger and /or Acquisition?

_____

_____

_____

10.What makes you unique in your firm's sector of operation

a) Assets i.e. I.T, Patents, Technology, Knowledge ☐
b) Market shares ☐
c) Organization i.e. people, culture ☐
d) Relationships ☐
e) Any other,please Specify

_____

SECTION 2

11.What is your firm's top goal?

a) Financial performance ☐
b) Service ☐
c) People ☐
d) Other(specify) ☐

_____

12.What do you hope to learn or have you learned from your merger and/or acquisition partner?

_____

13.Did this merger and/or acquisition bring in a new set of strategic assets such as :
products,people,goals,resources,processes,structures,advertising,distribution,customers,facilities,money) to help the new firm?

Yes ☐ No ☐

If Yes, what are they?

_____

_____

14.Do the two key management groups of the two firms that integrated through merger and /or acquisition blend well together?

Yes ☐ No ☐

15.Were any people with unique skills or expertise from the previous companie(s) retained in the new firm?

Yes ☐ No ☐

If yes, to 15 above, do specify the skills :

_____

16.Which activities that existed in the previous firm that was acquired or merged with have been integrated into the new business?

_____

17.What would you say about the products or services of the firms that merged or were acquired to create your firm?

☐ Complementary products
☐ Differentiated products
☐ Other - Specify: _____

18.What factors were considered in this Merger and/or Acquisition?
(May tick all as applicable)

☐ A perfect fit (synergy)

Please Specify: _____

☐ Geographic presence.

Please Specify: _____

☐ Organizational culture

Please Specify: _____

☐ Similar core competence

Please Specify: _____

☐ Synergies in research and development

☐ To improve growth and revenues

☐ To consolidate and be more competitive

☐ The political factors i.e antitrust laws

☐ Human factor

☐ Cost Reduction

Any other reason, please specify

_____

19. How compatible were the two firms of your Merger and /or Acquisition in the following aspects?

	Not Compatible	Moderate Compatibility	Very Compatible
a. Organization culture	☐	☐	☐
b. Management style	☐	☐	☐
c. Strategic assets i.e. products, people, goals resources, process & structures, advertising, distribution	☐	☐	☐
d. Goals and purpose	☐	☐	☐

20(a). List the areas of similarities between the two firms?

_____

_____

20(b) Do you agree that similarities allow sharing of knowledge and they also create opportunities?

Yes ☐ No ☐

21. Is the firm(s) you merged with or acquired a potential competitor or a provider of complementary goods?

Yes ☐ No ☐

22. Did you combine previously separate resources, positions, skills, and knowledge to contribute to differentiated resources, skills, brands, relationships and tangible assets in the new firm that would be said to create value?

Yes ☐ No ☐

If yes, specify:

_____

23.What statement best describes your revenues?

a) They were better before the merger ☐
b) Tremendous growth has been noticed after the merger ☐
c) Declining performance ☐
d) No noticeable change ☐
e) Any other comment (please specify) ☐

_____

24.What synergies came from the Merger and/or Acquisition ?
(*May tick as appropriate*)

a) Shared knowledge ☐
b) Shared tangible resources ☐
c) Pooled negotiating power ☐
d) Co-ordinated strategies ☐
if so specify:
_____
_____
_____
e) Vertical integration ☐
f) Combined new business creation ☐

25.Do you see your firm engaging in merging and/or acquisition in the near future?

Yes ☐ No ☐

If yes, specify:

_____

APPENDIX TWO

1.Do the firms learn from companies outside their businesses ?(seeQues.1 no.8)

In the Questionnaire 1,question 16 If yes are these activities important to the goal of the firm in question 7 & 11?

2.What is the purpose of the alliance? Is it by co-option or co-specialization ?(see questionnaire 1,questions no. 18,22,23)

3.From Questionnaire 1 ,question no.7, If distinctive technology was ticked, assess for learning and internalisation?

4.A critic of changes taking place in the various sectors that trigger Merger & Acquisitions any similarities or differences ? (see questionnaire 1.question no.2)

5.What inter- relationships among previously distinct business do we see across the sectors ? (See on questionnaire 1.,question no.13,14,15,16,17, , 18,21,22& 23)

6.Are there Merger & Acquisitions showing focus in their core business or diversity from question 6 above ?(see also Questionnaire 1,question no.9)

7.Compare and contrast differences or similarities between question 21 of Questionnaire 1 section two of all the seven sectors?

Find out whether the Shell/BP merger used the co-option alliance as was with the BP/Mobil merger in Europe?(see Ques.1 ,18&22)

8.Are there any trends across sectors for future Mergers and Acquisitions?(see Ques1,no. 26)