MERGERS AND ACQUISITION AND FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

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D53/MSA/PT/31545/2015

A RESEARCH PROJECT IN PARTIAL FULFILMENT OF THE REQUIREMENT FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION (FINANCE OPTION), KENYATTA UNIVERSITY

JUNE, 2022

DECLARATION

I hereby declare that the Project is my original work, and that it has not been submitted for any diploma or degree award at any other institution.

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DECLARATION BY THE SUPERVISOR

As the University Supervisor, I have approved the submission of this research project for examination.

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ACKNOWLEDGEMENT

Many thanks to the Almighty God for providing me with good health, strength, and guidance throughout the course of my research.

My heartfelt thanks go to my Father, Mother, and Brothers for their encouragement and unwavering support throughout the research period.

Dr. Peter Ng'ang'a of Kenyatta University's Department of Accounting and Finance and Coordinator of the School of Business deserves special recognition for his dedication, time, and effort in guiding me. Your ideas, suggestions, criticism, and advice are greatly valued. Without their assistance, this project would not have been possible.

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LIST OF ABBREVIATIONS

ACT	Agency Cost Theory
DEA	Data Envelopment Analysis
EPS	Earnings per Share
GDP	Gross domestic product
GSK	GlaxoSmithKline Kenya
KCB	Kenya commercial bank
M&As	Mergers and Acquisitions
NSCB	National Savings and Credit Bank
NSE	Nairobi Securities Exchange.
RBT	Resource-Based Theory
ROE	Return on Equity
ROCE	Return on capital employed
ROA	Return on Assets
SCA	Sustained Competitive Advantage
SSB	Social Security Bank

OPERATIONAL DEFINITION OF TERMS

Acquisitions refers to the change of ownership of

	businesses whereby companies form an alliance in order to maximize profits and improve their performance
Differential Efficiency	is attained when two companies in the same industry merge and efficiently utilize their resources
Financial performance	is a metric used to assess how well a company performs in terms of suing its assets to realize better returns
Market Share Development	refers to the increase in the customer and coverage base as a result of tow companies merging
Mergers	refers to the process of combining two companies into two
Organizational Operating Synergy	refers to the enhancement of business operations in order to reduce operational costs.
Risk Diversification	refers to the spread of business risks through diversifying the portfolios

ABSTRACT

Commercial banks' managers and shareholders are always adopting mergers and acquisitions aiming to improve their financial performance, economies, efficiency as well as their liquidity position. However, this doesn't always turn out to be so since different performances has been experienced by the firms that have undergone

mergers and acquisitions in the banking sector. While some studies indicate that mergers and acquisitions have adverse effect, others indicate that it doesn't have an effect while others have documented that it positively improves performance. In the recent years commercial banks have undergone mergers and acquisitions whereby in the last 20 years a total of 10 acquisitions and 13 mergers have taken place but the performance of these banks remain mixed. Therefore, there was a need to interrogate whether commercial banks' financial performance is affected by mergers and acquisitions given that the effect is mixed. The study's specific objectives included establishing the influence of organizational operating synergy, firm size and risk diversification as mergers and acquisitions effects on Kenyan commercial banks' financial performance. The theories that provided a theoretical justification as well as interrogation of the key study variables are; the Synergistic Mergers Theory, the Agency Cost Theory (ACT) and Resource Based Theory. A causal research design was adopted where a census was conducted on the entire population of the last 20 years' 10 acquisitions and 13 mergers. This study used both primary and secondary data, which was analyzed with SPSS to generate inferential and descriptive statistics and frequencies. The results of regression and correlation analysis were presented in tables and figures. The study found that organizational operating synergy, bank size, and risk diversification all had a positive and significant impact on the financial performance of Kenyan commercial banks. According to the study, operation synergy had a significant impact on bank financial performance due to lower operating expenses, increased market share, consolidation of operations, and synergies within the banking industry. An increase in bank size will result in effective gains that will be passed on to customers in the form of high deposit rates, lower lending rates, and lower interest rates. However, increasing the size of the bank beyond certain limits indicates a decline in the scale, leading to inefficiency. The diversification of a bank's operations varies depending on the bank. Diversification of risk is a risk-reduction technique that involves allocating investments across a variety of financial instruments. When banks diversify their risk, they reduce the amount of risk they are exposed to in order to maximize their returns. According to the study, Kenyan commercial banks should critically evaluate the merging institutions' overall business and operational compatibility and focus on capturing long-term operational synergies. There is a need for bank policies that place a higher priority on determining and monitoring their loan portfolio, customer deposits, and asset quality. The banks should invest in a broad range of assets such as bonds, stocks, real estate etc so as to reduce the volatility and risk to their portfolio by holding investments that have a low correlation to one another.

CHAPTER ONE

INTRODUCTION

1.1 Background to Study

Within the sector of banking, firms face performance challenges since most react to this challenges in a similar way. This is because most of the commercial banks offer similar products and services. In so doing, they face high competitions and as a result, they engage activities in pursuit of a competitive edge in order to keep their current customers and attract new ones (Porter, 2008). Some of the strategic activities these companies have engaged in the recent past have been Mergers and acquisitions.

According to (Ogada & Achoki, 2016), mergers are on an increasing trend in the Kenyan banking industry intensified after the financial crisis of 2008 as more regulatory bodies were formed to monitor banks performance. In the last decade, Mergers and Acquisitions (M & A) scope has been high and the drivers vary from business growth, changes in consumer's demand and the need to improve the delivery and financial position of the parties (Sharma, 2013). To have competitiveness and market share, firms are resorting to M & As. Furthermore, in order to diversify the risks in a firm's assets and penetrate new markets through economies, they use M & A (Kemal, 2014).

The bottom line for M & A has been placed on synergy where the belief that 2 are better than 1 takes the center stage (Sharma, 2013). For such with the belief that the wealth of the shareholders would improve, M & A takes place for the following reasons; economies, improved market share, synergy, geographical scope and revenues. Ownership matters has also pushed through the need for M & A as argued by Kemal

(2014). It has been argued that through M & a, firms would build their ownership size or separate their ownership thus delivering market power. In some cases, the expected benefits of M & A has been exaggerated and the shareholders end up flawed efficiencies.

In the last decade, a period termed as merger waves has seen a number of firm's experience M & A and the same can be attributed to the high failure rate for commercial banks in the USA (Berger, 2014). In other industries, acquisitions are being supported where people regard buying a ready existing business which is less risky and speedier to develop it than going through the process of organic growth in the USA (Jemison & Sitkin, 2015; Neale, 2013).

In Europe, M & As among financial institutions such as Germany has ended up in frustrations and decreased fortunes (Schmidt (2012). According to Augurzky *et al*. (2013), M & A pushes firms towards a monopolistic kind of operation citing examples whereby in the year 2011, the number of business owners had decreased to 1221 from 1399 in one of the sectors. As a result, they encouraged M & A rather than dropping out of the market (Sloan *et al*. 2013).

Ekungbe (2015) documents that the African setting doesn't have a lot of M & A activities. It's just recent because of globalization and popularity that the activity is gaining momentum. As a result, cross border acquisition has grown significantly (Rhodes-Kropf, Robinson & Viswanathan, 2015). In South Africa, the regulator of commercial banks prefers acquisitions to take place given the high failure of commercial banks in order to ensure a smooth transition.

In Ghana's banking sector M & As number has been increasing after Societe Generale. National Savings and Credit Bank (NSCB) and Social Security Bank (SSB) horizontal merger in May, 1994 resulted to this. Ghana has experienced more M & A transactions namely, United Bank of Africa in 2012, Access Bank in 2011 and Eco Bank in 2000. Jensen, Shleifer and Vishny (2013) have established that such factors like the need for value maximization, risk diversification and growth rate have led to M & As.

In Kenya, CBK of Kenya 2019 reports has shown that lately, there has been an increment in the quantity of M and A has expanded among Kenyan commercial banks, where it has been since 1989, the number of mergers among the commercial banks has been 34 and acquisitions has been 10. Some of the driving forces has been the need to meet the capital requirements, market share as well as competition in the operating environment (Appelbaum *et al*., 2014).

Existence of many local, viable and small owned competitors protect competition and passage by law cannot create it. Efforts will be put by antitrust laws in preventing actions reducing effective competitor numbers. According to the Restrictive Trade Practices, Monopolies and Price Control Act, merging of institutions is regarded against Kenya competition law background (Monopolies and Price Commission (MPC) Annual Report, 2015; Chesang, 2014).

1.1.1 Mergers and Acquisitions

This is change of ownership of businesses whereby companies form an alliance in order to maximize profits and improve their performance (Pazarkis *et al*, 2016). Gaughan (2013) refers to mergers as the process through which two firms come together. In an

acquisition, Nakamura (2015) indicates that part or the whole part of a business is acquired as a legal entity.

Conglomerate, vertical and horizontal form the three broad categories of mergers. Horizontal mergers occur when firms in the same sector or industry come together and it happens often where same business line firms merge to leverage on matching strategies. Such mergers improve market concentration of the firms (Scherer, 2013).

Vertical mergers on the other hand take place where firms in different sectors or industries come together such as buyer and supplier. In some scenarios, a merger may be between a manufacturing entity and the supplier of its raw materials with an aim of driving down costs or ensuring that there exist no supply interruptions (Samuels, 2015). Competition can be harmed by a vertical merger making it hard for new players to enter the market (Mueller, 2013; Muya, 2016).

The third type is conglomerates which occur between firms whose business lines are different. An example is a telecom company and a bank merger such as Safaricom and CBA bank. If not regulated, such mergers would kill competition and lead to monopoly which can harm the market (Mueller, 2013; Marsh, Siegel & Simons, 2016).

Mergers and Acquisitions play a significant role of accumulation of resources as well as human capacity and technology, synergy, efficiency, risk diversification and improving economies of scope and scale. Merged and acquired firms also have larger market shares which gives them a competitive edge over other players (Pazarkis *et al*, 2016).

1.1.2 Financial Performance

It indicates way in which a firm utilizes its assets to achieve better revenues. It measures the financial health of a business and is a method that can be used to compare performance across sectors or same sector. After an M & A, performance of its finances post M & A period is established through profits, liquidity, returns on equity and assets and solvency. If a company has been efficient after a merger, then its performance in terms of profits is expected to improve (Nakamura, 2015).

Even though there are various financial performance measures e.g ROE, ROA solvency, liquidity, profits and market share, this study will measure financial performance using ROE which has been regarded as the best method (Kemal, 2014). Furthermore, the measure is adopted because it is expected that after an M & A, the equity and assets of the companies increase hence it's prudent to establish the returns form equity.

1.1.3 Mergers and Acquisitions Effects on Financial Performance

One of the expected effects of M & A is improvement in an organizations competitive edge as well as improved market share, reduction in risk when entering in a new market as well as capitalizing on economies of scale to reduce costs (Saboo & Gopi, 2017). Other scholars link M & A to improvement in the employee's delivery and creation of team work. Through M & A, firms have been able to get the best from their employees (Ismail, Abdou & Annis, 2014).

Pazarkis *et al*. (2016) documented that M & A is said to have established value if the same would not have been achieved through change in control. The control is said to have benefits if it leads to redeployment of assets which brings forth new and operational

plans in the merger. Generally, the rationale behind M & A is synergy, enhanced revenues, growth in market share and sales, improvement on technology and market share.

The Agency theory however discourages M & A and argues that it leads to conflict of interest which has adverse effects on performance of the firm (Jensen & Meckling, 1976). The theory argues that M & A may not only bring about efficiency, but may also have adverse effects especially since the managers pushing for the M & A may be doing so to advance their own self-interests and agendas. It can be argued that managers may act on their own interests and force them a merger that will enhance their interests thus having an adverse effect on performance.

1.1.4 Kenyan Commercial Banks

CBK regulates Kenyan commercial banks forming the prudential guidelines for operations. At the moment, the Kenyan commercial banks licensed by CBK to operate in Kenya are 39. In the last ten years about 5 commercial banks have been placed under receivership because the competition in this sector has intensified

Mergers in this sector have increased over time compares to acquisitions although both have recorded increasing trends. By the year 2019, CBK reports indicates that since the year 1989, the number of mergers among the commercial banks has been 34 and acquisitions has been 10. In the last 20 years alone, a total of 23 commercial banks which are still operational have undergone merger/acquisition whereby 13 are mergers and 10 are acquisitions (CBK, 2019).

1.2 Study Problem

Managers of commercial banks and shareholders always adopt M & A with an aim of improving their financial performance, economies, efficiency as well as their liquidity position (Roll, 1986). However, this doesn't always turn out to be so since different performance mixed has been experienced by the firms that have undergone M & A in the banking sector. By the end of 2012, the Central Bank Of Kenya required banks to rise their core capital which forced them to begin discussions with each other. This led the shareholders and managers to consider mergers with the intention to improve financial performance. The study by Kenya & Konya (2015): Gathuku & Njeru (2015) looked at the ROA and ROE as a measurable dependent variable to measure performance. Others like Sonenshine & Reynolds (2014) used shareholder value, asset management and financial stability as their performance measure.

The effect of M & A is mixed whereby studies such as Selvam *et al*, (2009); Kling (2006); Ismail, Abdou & Annis (2010); King *et al*. (2004); Yeh & Hoshino (2002) document that it has adverse effects since it promotes conflict of interest among the managers of the firms. Other studies have documented that there is no significant improvement in either acquired or been merged firms' performance (Saple (2000). In a local context, Chesang (2017) similarly indicated that undergoing M & A has not improved the performance of commercial banks who have merged in the past. Others have documented that M & A has is the prerequisite for better performance and enhanced efficiency of the firms involved (Athanasoglou & Brissimis, 2004; Straub, 2007; Kithitu, *et al*, 2012).

CBK of Kenya 2019 reports has indicated that in the recent years, Kenya commercial banks' M & A number has increased since 1989, the number of mergers among the commercial banks has been 34 and acquisitions has been 10. However, despite that, the commercial banks continue to record mixed results thus creating a need to conduct this study and find out whether mergers and acquisitions affect financial performance of banks in Kenya. This is also relevant considering that the effect is mixed based on the previous studies.

1.3 Study Objective

1.3.1 Study General Objective

This research sought to determine how Kenyan banks' financial performance is affected by mergers and acquisitions.

1.3.2 Study Specific Objective

i. To establish the influence of organizational operating synergy as an effect of merger and acquisition on the financial performance of commercial banks in Kenya.

ii. To investigate bank size as an effect of merger and acquisition on financial performance of commercial banks in Kenya

iii. To assess risk diversification as an effect of merger and acquisition on financial performance of commercial banks in Kenya.

1.4 Study Questions

i. How does organizational operating synergy affect the financial performance of commercial banks in Kenya?

ii. To what extent does bank size affect financial performance of commercial banks in Kenya?

iii. How does risk diversification relate to financial performance of commercial banks in Kenya?

1.5 Study Significance

Banking sector in Kenya has recently witnessed an increasing number of M & A which can be narrowed down to the high competition in the sector. The study recommendations can hence play a role in guiding future decisions regarding M & A. Managers and executives in this industry can hence benefit from the study findings in that line.

The regulator of the banking sector, CBK, can also benefit from the recommendations. After the effect of M & A has been established and documented, the regulator may find it easy to come up with policies which may either encourage or discourage M & A for the benefit of fair competition in the sector and sustainable growth.

Investors willing and having targets of investing in this sector may find it important to understand whether the actions of M & A are beneficial or not to the firms. As a result, they may make informed decisions when suggesting for or against this practice in future.

It will add more insight into the relationship between mergers and acquisition with the financial performance to reseachers. Managers will use this information to have an indepth analysis of the financial performance in relation to the M & A.

Students and academicians will have a better understanding of mergers and acquisitions in the industry. They will use the study as a point of reference for any future research of M & A. Due to the fact that the areas still poses mixed results and that no specific focus has been seconded as such, the study is a good indicator of future research into the area in order to open up more deep understanding on the subject matter. Future studies will not only cite this work but also build on its shortcoming for a better and stronger theoretical basis.

1.6 Study Scope

The empirical interrogation' focus is whether M & A is crucial in enhancing performance and the specific focus of the work is operating synergy, bank size and risk diversification. The contextual focus was on all 23 Kenyan commercial banks that have been through acquisition/merging for the last 20 years until the time of study i.e. 13 banks that had undergone mergers and 10 banks that have undergone acquisition. The study was conducted in Nairobi as the headquarters of the 23 banks (CBK, 2019).

1.7 Study Limitations

Obtaining adequate data from banks' shareholders by the researcher may not be possible as it may prove hard in getting all the shareholder's adequate sample frame. However, the researcher ensured information on the shareholders' opinion on acquisition and merger issues is obtained comprehensively using the questionnaires.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter interrogates the study theme where the theoretical focus as well as the empirical studies in other contexts is presented. The chapter is important in highlighting the key areas in the determinants of firm profitability and growth that needs improvement thus justifying the need for this study.

2.2 Theoretical Literature

The theories that provide a theoretical justification as well as interrogation of the key study variables are presented and discussed in this Chapter. The theories range from the Synergistic Mergers Theory, Resource Based Theory and the Agency Cost Theory (ACT).

2.2.1 Synergistic Mergers Theory

Synergistic Mergers Theory was proposed by Bradley, Desai and Kim (1988). The theory presents an argument on the synergies arising as a result of a merger. Specifically, the theory presents a discussion of the financial and operational synergies as a result of a merger and acquisition. The theory posits that a firm enhances its synergy through a merger. Through M & A, firms are able to put together their operations and improve the efficiency even more.

According to Weston, Chung and Hoag (2003), firms are able to perform better after an M & A regardless of the type of merger. This is because of the assumption that before a

merger and Acquisition, a firm is performing below standard but after it, it is able to improve its operation. This is the concept of operating synergy.

In regard to financial synergy, the theory argues that the cost of raising funds externally reduces significantly. This improves their financial position and can enable them to adjust to their environment accordingly (Weston, Chung, & Hoag, 2003). Companies that have a small window for growth, may call for M & A because internal growth may be slower and take longer. The theory is important in explaining the role of M & A as a provider of synergy in firms thus being able to improve their operation as well as performance. The study supported risk diversification variable.

2.2.2 Resource Based Theory

The theory proposed by Wernefelt (1982) argues that the resources which firms have are critical to their performance. The theory emphasizes that the internal resources of a firm especially if they are valuable and unique, would play a role of bringing an edge for a firm over its competitors (Halpern, 2013).

Some of the studies that have adopted the theory in a similar study are Mugera and Bistch (2015), Gall and Shroeder (2014) and Ng (2007). In this study, the theory argues that M & A introduces a chance to build more on the resources of a firm which can then help push for its sustainable competitive edge over rivals. The resources will not only be financial or physical but also capabilities. With M&A, firms are able to build a source of financial power, the power of tangible resources and a group of employees who are competent to compete and have an edge over firms (Wang & Lo, 2013; Yarney, 2013). In the context of this study, the theory has been used to explain the role of mergers and acquisitions in enhancing efficiency and synergy. For the firms that are merging, the

firms can possess and exploit the resources and capabilities from both parties. This enables the firms to grow in terms of assets, capabilities, efficiency, effectiveness among many other ways for them exists a combined force to business at hand. Nonetheless, firms that acquire the weak firms have the financial muscle to take over. This brings about efficiency and the capabilities as well. The study supported risk diversification variable.

2.2.3 Agency Cost Theory (ACT)

Jensen and Meckling proposed the principal-agent theory in the years 1976 which contends that under states of fragmented data and vulnerability, which describe most business settings, two organization issues emerge: antagonistic choice and good peril (Eisenhardt, 2013). Unfriendly determination is the condition under which the chief can't find out if the operator precisely speaks to his capacity to take the necessary steps for which he is being paid. Moral danger is the condition under which the main can't make sure if the operator has advanced maximal exertion (Eisenhardt, 2013).

The issues of unfavorable choice and moral hazard imply that settled wage contracts are not generally the ideal approach to compose connections amongst principals and specialists (Jensen and Meckling, 1976). A settled wage may make a motivating force for the specialist to evade since his pay will be the same paying little heed to the nature of his work or his exertion level. At the point when operators have impetus to avoid, it is frequently more effective to supplant settled wages with remuneration considering lingering clamancy on the benefits of the firm (Alchian and Demsetz, 1972).

The foundation of a hybrid hierarchical frame does not take out all organization costs (Eisenhardt, 1989). Or maybe, the offer of lingering chaomancies on the benefits of retail outlets makes various new office costs, which originate from the administration of half and half hierarchical game plans. Office cost hypothesis develops one part of ICT, as it manages the alternate points of view of hazard that customer and provider have, and separates between result-based contracts, and conduct based contracts (Alchian and Demsetz, 1972). On the off chance that the customer questions the provider then the degree of checking required will be more prominent for the customer, than it would be if the customer could completely confide in the provider to convey. The customer has two fundamental options: an agreement which stipulates installment by comes about (a result-based contract), or an agreement that expresses the provider ought to do certain things at stipulated times or invest a specific measure of energy in specific capacities (Jensen and Meckling, 1976).

In relevance to this study, the theory proposes that M & A may not only bring about efficiency, but may also have adverse effects especially since the managers pushing for the M & A may be doing so to advance their own self-interests and agendas. It can be argued that the supervisors might act to their greatest advantage and hence force through a merger that will enhance their interests thus having an adverse effect on performance.

2.2.4 Market Power Theory

The Relative Market Power (RMP) hypothesis states that companies with large market shares and well-differentiated goods are more competitive and can earn above-average profits (Daddikar& Shaikh, 2014). An organization's financial output is really influenced by the composition of the asset. Will there be more existing assets or fixed assets in the

company? the idea of the theory is that the structure of an asset or its structure can make an organization more stable compared to its new competitors, its competitors or easily adapt to new technologies. The size of a company and its value are determined by the structure and the value of its properties. Smita (2011) argued that an organization should have the ability to preserve its principles and outwit its rivals, as per the 5 porter model. However, Athanasoglou (2009) observed that, through creativity, improving client relationships, smart recruiting practices, and acquiring rivals, companies appear to grow their market share. This is achieved by strategizing established competitors, new market entrants, the power to sell and buy goods, and has unique features of products, particularly for closely replaced products. Normally, restructuring allows an organization to amass resources in a pool in order to increase the entity's capital base. Khan (2011) claimed that it can easily diversify its operations and goods when an entity enjoys the economy of scale by consolidation by combining operations. Yusuf (2016) also stated that after diversification, market penetration would boost the consumer base, as a result of more transactions and customer-enjoyed powerful technology, asset structure has changed. To win the market, a company must be able to produce efficiently (Kiplangat, 2006). The correct quantity of goods at the right time and at a lower rate without affecting their value. An organization would be encouraged to amalgamate when the merger capital adequacy of the commercial bank and the potential cash flow are strong (Marangu, 2007).

2.2.5 Efficiency Theory

The theory supports the takeover of inefficient firms and the survival of successful ones by focusing on the Michael Porters model for businesses that focus on improving market

share (Beck, 2010; Bemile, 2011). The bank's capital is the foundation for growth and, in practice, the need for the business to plan for sound investments with positive returns. In order to protect depositors' rights and interests, banks are required to maintain a minimum capital reserve with the Kenyan Central Bank. Therefore, in this situation, productive companies can function at maximum production capacity with minimal production costs. Commercial banks need to have a well-qualified and skilled workforce to maintain and have a greater market share, well vast with a market climate, improving the value and efficiency of the organization (Sharma, 2009). New information on new entrants, buyer and seller bargaining power, and nearby product alternatives must be managed in order to achieve an effective market share resulting in improved operating resources.

As per the efficient market theory, a market would contain the sum of every investors' market views, to which the stock market would respond quickly (Beck, 2010). Hu (2009) concluded that mergers produce enough unity to make the deal viable for both parties. To maximize the value of the shareholders, the goods must be cost-effective in order for the company to be profitable. Mishra (2010) contended that the efficiency theory produced positive returns on financial results as a result of an organization's value formation. This is done by development beyond the frontier of production possibility (PPF) that would not use the available resource either under or above. Pike (2006) argued that managers who do not generate to completely optimize income along the PPF curve will direct their efforts toward goals other than improving financial efficiency, which is inimical to the interests of shareholders It should be noted, however, that well-informed opportunistic investors may observe poorly performing businesses with strong discipline and assets and

combine with poorly performing organizations by enhancing them to increase their market share. Thus, as new hires become aware of the full potential of the assets of a target by improving their output by minimizing costs (Sathye, 2005). The theory of synergistic mergers suggests that company managers can increase their productivity by unifying their sector with competent target companies and then improving their financial returns (Pandey, 2008; Pike, 2006). As a result of the synergistic effect of consolidating with the buyer firm, it should improve its performance even further (Pasiouras, 2007). The study supported bank size variable

2.3 Empirical Literature Review

The section presents a review of other studies on the main study themes as presented. By focusing on a review of other studies, it guides development of research gaps which sought to address. It covers the correlation between organizational operating synergy, risk diversification and bank size with performance.

2.3.1 Organizational Operating Synergy and Performance

Davidson, Frank and Ismail (2009) interrogated whether M & A was a critical factor of European bank performance basing data on a five-year period. Through an event study, it was determined that the main performance indicator had not registered substantial improvement even after the merger. The operations and rules governing operations of commercial banks in Europe are quite different from that of this study hence the study's findings cannot be applied to Kenya. There is a contextual gap between the study and this study.

Lazaridis (2003) interrogated whether indeed the M & A taken with an aim of enhancing efficiency and synergy achieved the same. Through a quantitative survey, it was determined that indeed the synergies improved after the M & A. The study suggested that indeed there is always a firm willing to engage and acquire an underperforming one and improve its performance to greater levels. The study was however contextually different from this study and the findings cannot be generalized to the Kenyan setting since the operations in Greece are different from that of Kenya.

Andre, Kooli and L'Her (2014) set to establish how a number of commercial banks in Canada had faired on after their mergers. This study only looked at mergers of the commercial banks. The data set adopted spanned 1980 to 2000 and through t-tests, the study discovered that after the M & A, these entities underperformed overwhelmingly. The study was however contextually different from this study and the findings cannot be generalized to the Kenyan setting since the operations in Canada are different from that of Kenya.

In another interrogation, Agrawal, Jaffe and Mandelker (2012) in their study focused on a total of 937 firms to interrogate the same concept and revealed that the firms improved their returns after M & A in the long run. The study however focused on listed firms only while this study does not narrow down to listed firms only.

Similarly, in Uk, Ingham, Kiran and Lovestam (2011) established the performance of mergers among top 500 firms not necessarily commercial banks. It was indicated that the period post-merger demonstrated a good performance for these firms. Furthermore, it was more likely where the integration of smaller firms into larger firms happened. Compared

to this study, this study presents a contextual gap since the focus on UK non-banking firms cannot be generalized to Kenyan banking firms.

Firth (2013) analyzed the shareholders returns and management benefits after a merger for UK based firms using a descriptive study. The acquired firms demonstrated to bring more benefits and returns. However, the acquiring firms demonstrated great losses especially in cases where the motivating factor was maximization of shareholders benefits. Compared to this study, this study presents a contextual gap since the focus on UK non-banking firms cannot be generalized to Kenyan banking firms.

2.3.2 Risk diversification and Performance

Altunbas and Ibanez (2004) interrogated whether M & A ensued into better performance and reduced risks among UK based firms. The study focused on individual bank mergers data and ran empirical analysis which established that after the mergers, the results indicated that when smaller firms merged with larger firms, the smaller firms benefited even more because they are able to accumulate more capital. Furthermore, they were able to diversify their risks which enhanced their chances of better performance. The study, however, was conducted in a different context of the UK which is developed thus indicating a contextual difference to mean that the findings cannot be generalized to Kenya.

Lamont and Polk (2009) interrogated whether M & A enhanced cash flows and improved returns after. They demonstrated that when it happens within the same segment, the firms recorded more returns as compared to if it was conducted across segments. It was also shown that cash flow improved after the M & A. The study presented a conceptual gap

since the focus was on how M & A affects cash flow and returns and not the measures of performance indicated in this study.

Villalonga (2000) focused on US based listed firms and established whether M & A improved their diversification risks. It was revealed that after the M & A, the firms were able to diversify their portfolio even more an indication that they reduce their diversification risks accordingly. The study was however a study conducted in a different context of US which is developed thus indicating a contextual difference to mean that the findings cannot be generalized to Kenya.

Franks, Harris, and Titman (2011) focused on a similar theme but on 399 firms in time period spanning 1975-1984. Even though the time of the study greatly differs with this study, it contributed relevant information to the topic by indicating that after the M & A, the firms recorded an improvement in stock returns but only in the short run to imply that after the merger, the firms may inherit benchmark errors which may affect performance adversely. The study however focused on listed firms while this study focuses not just listed but also firms which have not been listed at NSE. This is a methodological gap.

Palia (2012) conducted a study with a different conceptual approach from this one by establishing the factors which hindered merging among commercial banks. It was demonstrated that among the factors, the level of risk in diversification, equity ownership, asset quality and capital risk played a significant role in the decision to merge. It was established that the level of risk of the merging firms played a significant role in the decision.

Locally, Muthiani (2015) adopted the opinions of the managers on whether the M & A conducted by GlaxoSmithKline Kenya PLC (GSK) had been significant on their performance. It was established that even though the process was influenced by organizational culture, the process enabled the firm to reduce its diversification risks. In the long run, the M & A had helped improve performance. The study was however a case study which presents a methodological deviation from this interrogation.

In the commercial banks sector, similar to this interrogation, Chesang (2015) found out whether M & A improved the financial aspect of the parties involved. The study moderated for the relationship through firm size but however revealed that commercial banks performed how they did regardless of whether they merged or not since they operate under similar conditions and regulated by the same prudential rules. Compared to this study, the study involved a moderating variable which indicated a conceptual diversity from this study.

Muya (2016) in a similar focus established that M & A were not in way significant determinants of the financial performance of firms. It specifically revealed that it doesn't add any value to the performance of the parties involved hence it was not recommended. In the context of coffee marketing societies, Njenga (2016) demonstrated that M & A was not crucial to their operations and was hence not advised. The two studies differ from this study based on the context they were conducted. The focus was on non-financial setup hence the results cannot reflect what is happening in a financial setting being governed by CBK rules.

2.3.3 Bank Size and Performance

Rhoades (2003) interrogated 33 banks that had undergone M & A to find out if their size enhanced efficiency and profitability. It was indicated that the cost efficiency improved due to economies of scale after the merger. Resti (2008) interrogated whether M & A was critical in enhancing efficiency through economies. The descriptive interrogation demonstrated that the firms were able to benefit from economies of scope and scale and hence it was concluded that indeed M & A was critical in building on size and enhancing efficiency. The contextual focus of the studies compared to this study is different whereby as they looked at developed economies, this study focuses on an emerging economy.

Reda (2013) through Data Envelopment Method, focused on banks in Egypt to find out whether efficiency was obtained using economies attributed to size after a merger. With data between 2000 and 2003, the study established that the banks improved their cost efficiency significantly after the M & A since most of them had quality assets. Loderer and Martin (2010) based their study on a total of 304 mergers using data collected on a 2o year period up to the year 1986 and indicated that the firms that had merged recorded significant improvement in size but did not perform better due to inefficiencies. The contextual focus of the studies compared to this study is different whereby as they looked at developed economies, this study focuses on an emerging economy.

Ansof, Bradenburc, Porter and Radosevlch (2011) demonstrated that after the merger, firms which were previously showing low growth in sales started showing a high growth while those that were showing a high growth, indicated slightly diverse growth. Locally, Muchae (2014) established whether Tiger Brands Cross border M & A was critical to

their performance. It was demonstrated that motivation among the staff decreased sharply after the merger because of matters related to job security and that affected performance significantly. Muchae (2014) used a case study design in his study, whereas this study focuses on a survey, thus presenting a methodological gap since a case study is not satisfactory in eliciting diverse opinion and reaching a far in-depth conclusion.

Focusing on financial players in the UK, Haynes and Thompson (2005) investigated for the presence of M & A and its effect. The effect was tested on specifically sales and market share. Through unbalanced panel data of 93 firms, it was indicated that there is no discernible and observable value of M&A on the firms that have gone through it. King et al. (2004) on the other hand employed a meta-analysis in their interrogation of impact of M & A where only published materials were focused on. It was demonstrated after the review that even though the M & A improved market shares and size, it was not found to be a significant predictor of superior performance. In Greece, Pazarskis et al. (2006) through a questionnaire on the listed firms at Athens, indicated that M & A improved the firm size and market share which further enhanced their performance. The contextual focus of the studies compared to this study is different whereby as they looked at developed economies, this study focuses on an emerging economy.

2.4 Summary and Gap

The performance of the mergers and acquisitions for acquiring firms has been widely investigated. Researchers focused on the circumstances leading to and what would be the short and long term gains on either the acquired or acquired firms. Additionally, the market for corporate control and performance of acquiring firms has been investigated by fellow researchers. All of mentioned research focused on before and after effects of the

individual parties in the M & A process but this study investigates the long term performance after the process. This constitutes a conceptual research gap which this study is seeking to close.

Other studies have presented contextual research gaps. The study by Davidson, Frank and Ismail (2009) focused on European banks, Andre, Kooli and L'Her (2014) focused on Canadian mergers and acquisitions, Ingham, Kiran and Lovestam (2011) focused on UK's top 500 companies, Franks, Harris, and Titman (2011) focused on USA based firms while Reda (2013) focused on Egyptian banks. The findings from these developed economies cannot be generalized to the Kenyan context hence a need for this study.

Table 2.1: Summary and Gap

Name	Year	Title	Results	Gaps
Rhoades (2003)	2003	Impact of M & A on Efficiency and Profitability of banking firms	Merger did not have a significant effect on efficiency	The study specifically focused on both efficiency and performance while this study focuses on efficiency as an independent variable
Haynes and Thompson (2005)	2005	Effect of M & A on Market Share among Financial players in UK	Mergers significantly improved the market share among UK financial mutual sector	The study linked mergers to market share while this study links it to performance
Haynes and Thompson (2005)	2005	Effect of M & A on Market Share among Financial players in UK	Mergers significantly improved the market share among UK financial mutual sector	The study linked mergers to market share while this study links it to performance

Name	Year	Title	Results	Gaps
Pazarskis *et al.* (2006)	2006	The effect of mergers and acquisitions on operating performance in Greek firms	Mergers and acquisitions fundamentally affect firm work performance.	The study focused on the context of developed economy hence findings cannot be generalized to Kenya
Ingham, Kiran and Lovestam (2011)	2011	M & A and performance of UK's top 500 companies	mergers and firm profitability didn't have a significant change	The study focused on the context of developed economy hence findings cannot be generalized to Kenya
Agrawal, Jaffe and Mandelker (2012)	2012	Post-merger performance of acquiring firms	Following the merger, the acquiring firms performed better.	The study focused on the context of developed economy hence findings cannot be generalized to Kenya
Palia (2012)	2012	Factors influencing the level of bank merger premiums focusing on financial and regulatory factors.	Regulatory factors affected banker merger premiums significantly	The study investigated the factors that influence the level of bank merger premiums and not its effect on performance
Andre, Kooli and L'Her (2014)	2014	Interrogating the Long term performance of M & As in Canadian context	The performance of mergers and acquisitions did not change significantly.	The study focused on long-term performance rather than short-term performance.
Muchae (2014)	2014	Determinants and influence of cross border M & A in Tiger	Regulatory and cultural differences affected	The study concentrated on the difficulties associated with

Name	Year	Title	Results	Gaps
		Brands Limited	mergers and acquisitions across borders	cross-border mergers and not its effect on performance.

Source: Research Da

2.5 Conceptual Framework

The conceptual framework is a metaphorical way of showing how the concepts in a survey are related (Creswell, 2012). The diagram below represents the variables that will be investigated by the study. The diagram below represents the variables that will be investigated by the study.

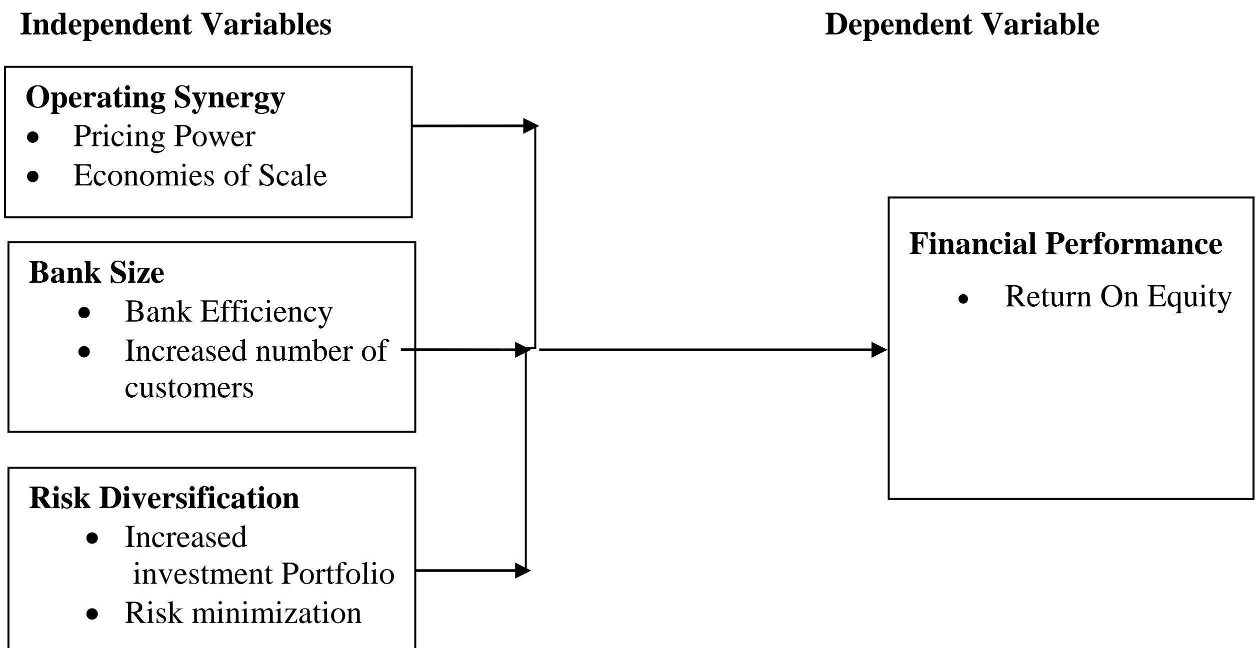


Figure 2.1: Conceptual framework

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

Research methodology interrogates the procedures through which a research is performed (Kothari, 2004). The methodology to be adopted in this study is highlighted in this chapter and ranges from the sampling, adopted design, population and data collection and analysis procedures.

3.2 Research Design

According to (Zikmund et al, 2013) research design provides a framework of the research. A causal design was adopted, Gay and Airasian (2003) supports this approach as better positioned to indicate the relationships between variables in a study. In this study, how M & A affects financial performance is better established using this design. Causal design is basically an outline that guides the researcher when collecting, measuring and analyzing data and the intent of research design is to guide the whole process of research. As a result, the design aided in obtaining current status information on how Kenyan banks' financial performance is affected by mergers and acquisitions.

3.3 Study Population

Population is the entire study units to be interrogated (Hungler and Pilot, 1999). In this study, the commercial banks which had gone through acquisitions and mergers in the last twenty years will be targeted. A CBK (2019) report documented that for the last 20 years, a total of 13 mergers and 10 acquisitions of commercial banks (see appendix IV) which

were still operational to date has taken place as summarized in Table 3.1. From each commercial bank, the target respondents were heads of finance, human resource, marketing, operations, administration, retail banking and IT departments.

Table 3.1: Study Population

Category	**Population**	**Percentage**
Mergers	13	57
Acquisitions	10	43
Total	**23**	**100**

Source: CBK (2019)

3.4 Sample Technique and Size

The study took a census of the 23 commercial banks that have merged or been acquired in Kenya's banking industry. A census was considered suitable according to Smith (2015) who argued that a census is suitable when the target population is smaller than 100. The unit of observation was however purposively sampled as the heads of finance, human resource, marketing, operations, administration, retail banking and IT departments of the commercial banks. A total of 7 respondents was sampled from each of the 23 commercial banks leading to a total of 161 respondents.

3.5 Study Instrument

Data from primary as well as secondary sources was used in achieving the objectives. A structured questionnaire using in a Likert scale was utilized in collecting primary data. A secondary data sheet from the CBK reports (Appendix III) was used to collect secondary data (commercial banks' financial performance). The secondary data was collected on a time period of 5 years.

3.6.1 Research Instrument Validity

Reliability is consistency through which an instrument measures the same phenomena in repeated trials (Hungler & Pilot, 1999). There was a need to ensure that the questionnaire is reliable before being used and hence the researcher conducted an internal consistency test. In this test, a Cronbach Alpha was used where a value above 0.7 was used to indicate reliability.

3.6.2 Research Instrument Reliability

Validity indicates whether the research instrument measures meaningful information (Smith, 2015). This process is not statistical and hence the study measured validity through expert opinion where the experts in finance as well as university supervisors gave their opinion on the questionnaire for adjustments from the pilot test.

3.7 Procedure in Collecting Data

The procedure for collecting data varied from secondary data to primary data collection. Drop and pick method was applied in collecting primary data. On the other hand, secondary data collection was by use of a secondary data sheet, bank's financial statements, annual reports and CBK reports was used in obtaining the information. Before data collection, a letter from the university was obtained to enable application of NACOSTI and then permission was sought from the commercial banks before the process begins. Data was collected in a span of 2 months.

Table 3.2: Results of Reliability Tests

Study Variables	Alpha (α) Value
Operating Synergy	0.798
Bank Size	0.803
Risk Diversification	0.811
Financial performance	0.799
Average Score	**0.799**

Source: Pilot Study (2021)

The following reliability results were obtained using SPSS 21.0: operating synergy, bank size, risk diversification, and financial performance, with Cronbach alpha values of 0.798, 0.803, 0.811, and 0.799. The average alpha coefficient for each individual variable was significantly higher than 0.7, confirming Mugenda and Mugenda (2003)'s recommendation that an alpha coefficient score of more than 0.7 indicates that the instruments are highly reliable. According to Hazzi and Maldaon (2015), an alpha coefficient ranging from 0.75 to 1.0 is considered reliable for the obtained results. As a result, the obtained average Cronbach's Alpha Index () value of 0.799 was acceptable because it was within the acceptable range.

3.8 Data Analysis and Presentation

This is the procedure of processing raw data into information that can be interpreted easily (Sounders, Lewis & Thornbill, 2009; Burns & Grove, 2003; Hyndman, 2008). The information gathered in the field was edited and coded in Excel. It was then transferred into SPSS and analyzed where descriptive such as mean, standard deviation will be

established. Correlation and regression was on the other hand adopted to indicate the relationships. The regression model was in the form:

$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon$

Where:

Y = Financial Performance

X_1 = Organizational Operating Synergy

X_2 = Bank size

X_3 = Risk Diversification

ε = error

β_0 = constant

$\beta_1 - \beta_4$ = coefficient

3.9 Operationalization and measurement of Variable

ROA was chosen as the performance metric for Kenyan commercial banks for the purposes of this study. The independent variables include operating synergy, bank size and risk diversification. Below table shows summary of data operationalization for the study.

Table 3.3: Operationalization and measure of Variable

Variables	Types	Operationalizations	Measurements
Financial Performance	• Dependent	• ROE • ROA	Profitability
Operating Synergy	• Independent	• Pricing Power • Economies of Scale	5 likert scale questionnaire
Bank Size	• Independent	• Bank Efficiency • Increased number of customers	5 likert scale questionnaire
Risk Diversification	• Independent	• Increased investment Portfolio • Risk minimization	5 likert scale questionnaire

Source (Research data, 2020)

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSION

4.1 Introduction

This chapter presents the results of field data collected from the field in chapter 3. It was then analyzed to determine if there was a difference in the financial performance as measured by ROA and ROE.

4.2 Response Rate

The study had a sample population of total of 161 respondents. Questionnaires were administered to each of these respondents.

Table 4.1: Response Rate

Category	Frequencies	Percentages
Respondent	155	96.3
No response	6	3.7
Total	**161**	**100**

According to Table 4.1, the response rate is 96.3 percent, and the non-response rate is 3.7 percent. According to Baruch (2012), a response rate of more than 80% is sufficient to analyze the data. As a result, a study response rate of 96.3 percent was deemed appropriate for data analysis. This meant that the study's research findings were accepted and credible as a result of the high response rate.

4.3 Background Information

The research focused on respondents' background information in terms of work experience, department and the number of employees in their organization. The results are summarized below:

4.3.1 Work Experience

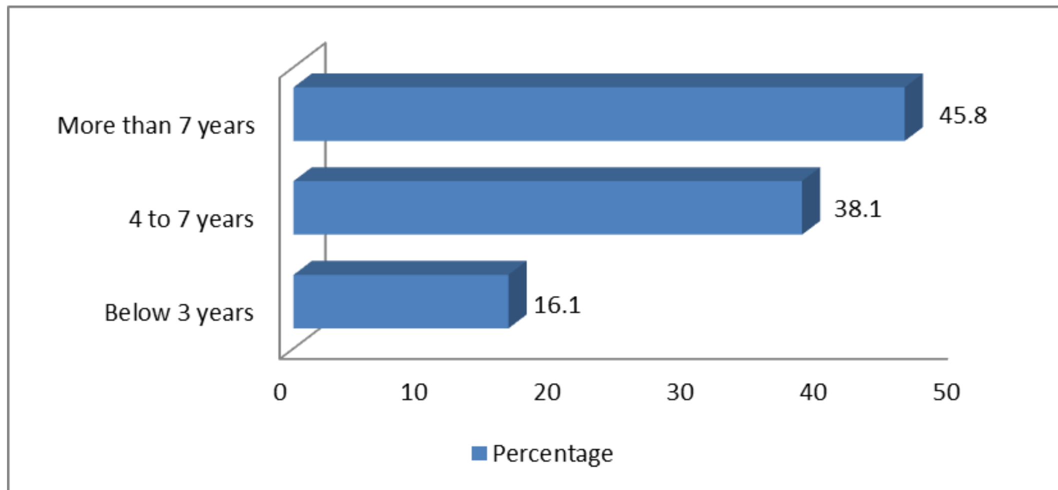


Figure 4.1: Work Experience

According to Figure 4.1, the majority of respondents (45.8 percent) had more than 7 years of work experience, 38.1 percent were 4 to 7 years old, and 16.1 percent were less than 3 years old. These findings confirm that participants in this study have the necessary experience to provide information about how Kenyan banks' financial performance is affected by mergers and acquisitions.

4.3.2 Department

The study wanted to know how the respondents in the study were represented in terms of their departments.

Table 4.2: Department

Department	Frequencies	Percentages
Human resource	32	20.6
Information technology	10	6.5
Finance	21	13.5
Marketing	15	9.7
Operations	26	16.8
Administrations	18	11.6

Retail banking	33	21.3
Total	**155**	**100**

It found that most of respondents (21.3%) were from the retail banking department. 20.6% of the respondents were from the department of human resource, 16.8% operations department, 13.5% finance, 11.6% administrations, 9.7% marketing and 6.5% information technology. It was necessary to obtain the respondents from different departments so as to get a diverse perspective on how merger and acquisition affects financial performance in all the banks departments.

4.4 Results of Descriptive Analysis

To present the results of the quantitative data, descriptive statistics included Mean (M) and Standard Deviation (SD). The outcomes are shown below.

4.4.1 Organizational Operating Synergy

Table 4.3: Organizational Operating Synergy

Statements	M	SD
The merger activity has improved economies of scale	4.08	1.157
The merger activity has improved economies of scope	4.05	0.828
The merger activity has improved pricing power	4.30	0.598
The merger activity has improved the marketing power	4.12	0.836
The merger activity has improved the levels of growth	4.55	0.515
Aggregate Score	**4.15**	**0.894**

Source: Survey Data (2021)

According to the results in Table 4.3, respondents agreed that organizational operating synergy as a result of merger and acquisition influences the financial performance of Kenyan commercial banks, as evidenced by an aggregate of 4.15 and a standard deviation of 0.894. This agrees with Ingham, Kiran and Lovestam (2011) study that established the

performance of mergers among top 500 firms not necessarily commercial banks and indicated that the period post-merger demonstrated a good performance for these firms. Furthermore, it was more likely where the integration of smaller firms into larger firms happened. Compared to this study, this study presents a contextual gap since the focus on UK non-banking firms cannot be generalized to Kenyan banking firms.

The statements strongly agreed by the respondents were; the merger activity has improved the levels of growth (M=4.55, SD=0.515). This correspond to Firth (2013) study that analyzed the shareholders returns and management benefits after a merger for UK based firms using a descriptive study. The acquired firms demonstrated to bring more benefits and returns. However, the acquiring firms demonstrated great losses especially in cases where the motivating factor was maximization of shareholders benefits.

The statements agreed were that; the merger activity has improved pricing power (M=4.30, SD=0.598), the merger activity has improved the marketing power (M=4.12, SD=0.836), the merger activity has improved economies of scale (M=4.08, SD=1.157) and that the merger activity has improved economies of scope (M=4.05, SD=0.828). The support the argument by Davidson, Frank and Ismail (2009) who interrogated whether M & A was an important factor of the performance of European banks basing data on a five-year period. Through an event study, it was determined that the main performance indicator had not registered substantial improvement even after the merger.

4.4.2 Bank Size

Table 4.4: Bank Size

Statements	M	SD
The company has made use of economies of scope to manage costs	4.50	0.790

The company has made use of economies of scale to manage costs	3.23	1.726
As a result of acquisition and merger activity many branches have been established by our institution	3.94	1.068
The number of customers has increased after the merger	4.84	0.749
Capital adequacy requirements has improved after the merger	4.04	1.707
Aggregate Score	**4.35**	**0.65**

According to the results in Table 4.4, respondents agreed that the size of the bank as a result of merger and acquisition affected the financial performance of commercial banks in Kenya, as evidenced by a total of 4.35 and a standard deviation of 0.65.This concurs with Loderer and Martin (2010) who based their study on a total of 304 mergers using data collected on a 2o year period up to the year 1986 and indicated that the firms that had merged recorded significant improvement in size but did not perform better due to inefficiencies.

The statements strongly agreed were; that the number of customers increased as a result of the merger (M=4.84, SD=0.749) and that the company has made use of economies of scope to manage costs (M=4.50, SD=0.790). This is in consistent with the results of Ansof, Bradenburc, Porter and Radosevlch (2011) study that demonstrated that after the merger, firms which were previously showing low growth in sales started showing a high growth while those that were showing a high growth, indicated slightly diverse growth. Locally, Muchae (2014) established whether Tiger Brands Cross border M & A was critical to their performance. It was demonstrated that motivation among the staff decreased sharply after the merger because of matters related to job security and that affected performance significantly.

The respondents agreed on the statements that capital adequacy requirements has improved after the merger (M=4.04, SD=1.707) and that as a result of acquisition and

merger activity many branches have been established by our institution (M=3.94, SD=1.068). This concurs with the findings of Resti (2008) study that interrogated whether M & A was critical in enhancing efficiency through economies. The descriptive interrogation demonstrated that the firms were able to benefit from economies of scope and scale and hence it was concluded that indeed M & A was critical in building on size and enhancing efficiency.

Respondents indicated a moderate level of agreement with the statement that the company has made use of economies of scale to manage costs (M=3.23, SD=1.726). This does not support the findings by Rhoades (2003) study that interrogated 33 banks that had undergone M & A to find out if their size enhanced efficiency and profitability. It was indicated that the cost efficiency improved due to economies of scale after the merger.

4.4.3 Risk Diversification

Table 4.5: Risk Diversification

Statements	M	SD
As a result of acquisition and merger activity many branches have been established by our institution	4.65	0.470
Following the merger, new branches were established, resulting in the expansion of the market portfolio.	4.05	0.760
Product portfolio has increased after the merger because of the formation of new branches	4.28	1.136
Investment portfolio has increased after the merger because of the formation of new branches	4.75	0.734
Following the merger, new branches have attracted a diverse human resource portfolio.	3.58	0.734
Aggregate Score	**4.55**	**0.450**

According to the results in Table 4.5, respondents strongly agree that the risk variance due to merger and acquisition affects the financial performance of Kenyan commercial banks, as evidenced by the amount of 4.55 and the standard deviation of 0.450. This is

supported by the findings of Muthiani (2015) study that adopted the opinions of the managers on whether the M & A conducted by GlaxoSmithKline Kenya PLC (GSK) had been significant on their performance. It was established that even despite the fact that organizational culture played a role in the process, the process enabled the firm to reduce its diversification risks. In the long run, the M & A had helped improve performance.

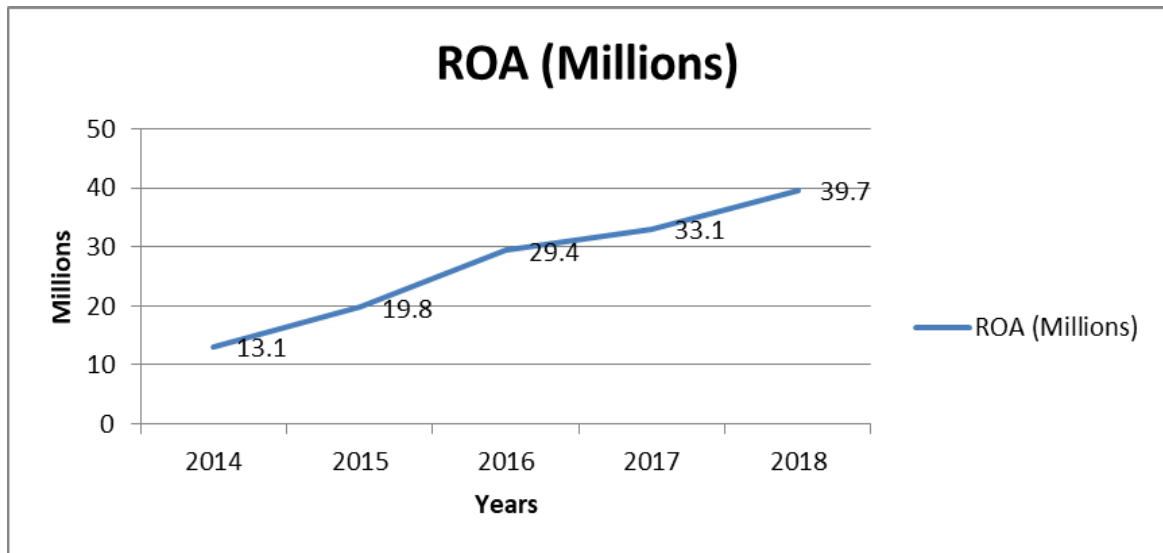
The statements with the highest mean were that; investment portfolio has increased after the merger because of the formation of new branches (M=4.75, SD=0.734) and that as a result of acquisition and merger activity many branches have been established by our institution (M=4.75, SD=0.470). The findings supports Chesang (2015) study that found out whether M & A improved the financial aspect of the parties involved. The study moderated for the relationship through firm size but however revealed that commercial banks performed how they did regardless of whether they merged or not since they operate under similar conditions and regulated by the same prudential rules.

The respondents agreed on the statements that product portfolio has increased after the merger because of the formation of new branches (M=4.28, SD=1.136), the establishment of new branches following the merger has resulted in the expansion of the market portfolio (M=4.05, SD=0.760) and that following the merger, new branches have attracted a diverse human resource portfolio (M=3.58, SD=0.734). The finding support Palia (2012) who conducted a study with a different conceptual approach from this one by establishing the factors which hindered merging among commercial banks and it was demonstrated that among the factors, the level of risk in diversification, equity ownership, asset quality and capital risk played a significant role in the decision to merge.

4.4.4 Financial Performance

The study sought to determine the extent to which mergers and acquisitions influenced the financial performance of Kenyan commercial banks. The outcomes are shown in Figure 4.2.

Figure 4.2: Financial Performance



Source: Survey Data (2021)

As shown in Figure 4.2, the financial performance of Kenya's commercial banks continued to increase from the year 2014 to 2018 from 13.2 million Kenyan shillings to 39.7 million Kenyan shillings. This is an indicator that mergers and acquisitions enabled the banks to increase in their ROA for the lastPazarkis *et al.* (2016) study documented that M & A is said to have established value if the same would not have been achieved through change in control. The control is said to have benefits if it leads to redeployment of assets which brings forth new and operational plans in the merger. Generally, the rationale behind M & A is synergy, enhanced revenues, growth in market share and sales, improvement on technology and market share.

4.5 Results of Inferential Analysis

4.5.1 Correlation Analysis

Table 4.6: Correlation Analysis

		Organizational operating synergy	Bank Size	Risk Diversification	Financial Performance
Organizational Operating synergy	Pearson Correlation	1			
	Sig. (2-tailed)				
	N	88	1		
Bank size	Pearson	.109			
	Correlation	.341	88		
	Sig. (2-tailed)				
	N	88			
Risk diversification	Pearson Correlation	.080	.711**	1	
	Sig. (2-tailed)	.485	.000		
	N	88	88	88	
Financial performance	Pearson Correlation	.741**	.853**	.606**	
	Sig. (2-tailed)	.000	.000	.000	
	N	88	88	88	

Source: Survey Data (2021)

The correlation coefficient for the four study variables is shown in Table 4.6. According to the table, all of the correlation coefficients are statistically significant at the 0.01 level of significance for the two-tailed test. The correlation coefficients for organizational operating synergy, bank size, risk diversification and financial performance against strategy implementation were found to be 0.7411, 0.853 and 0.606 respectively indicating that the variables have a strong positive linear relationship.

These findings is in line with Davidson, Frank and Ismail (2009) who interrogated whether M & A was so crucial in determining the performance of European banks basing data on a five-year period. Through an event study, it was determined that the main performance indicator had not registered substantial improvement even after the merger. The finding support Chesang (2015) study that found out whether M & A improved the financial aspect of the parties involved. The study moderated for the relationship through firm size but however revealed that commercial banks performed how they did regardless of whether they merged or not since they operate under similar conditions and regulated by the same prudential rules.

4.5.2 Regression Analysis

The effect of one variable on the other was determined using regression analysis. This was realized by regressing organizational operating synergy, bank size, risk diversification on financial performance.

Table 4.7: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.636	0.805	0.772	0.454

A summary of the model is shown in Table 4.7, which includes information about the retrospective linear narrative capability for the full range of dependent variables. R is the ratio of the strength of the relationship between dependent and independent variables and is represented by a factor of 0.636, which is close to one when both dependent and independent variables are closely related. The coefficient of determination, also known as R2, is a mathematical estimate of how close the data is to the embedded downtime. The

greater the square root of R, the better the model and the research data. As a result, the optimal study accuracy is 0.805 (80.5%) to 0.805 (80.5%).

The results in Table 4.7 also show that 0.805(80.5%) is the value of adjusted R square indicating the extent to which the independent variables studied, which included organizational operating synergy, determined the financial performance of commercial banks in Kenya, bank size and risk diversification. Therefore, the remaining percentage (19.5%) represented other factors on studied.

Table 4.8: Analysis of Variance

Model		Sum of Squares	Df	Mean Square	F.	Sig.
1	Regression	10.387	4	2.597	12.572	0.000[a]
	Residual	15.284	151	0.207		
	Total	25.671	155			

The value of 0.000a indicates that the value level is less than 0.05, which indicates that the model is statistically significant depending on how the independent variables tested have impacted the financial performance of commercial banks in Kenya. At the value of 5%, the calculated value of F (12.572) is greater than the value set in table F (2.597), confirming the value of the model.

Table 4.9: Coefficients

Model		Unstandardized Coeficient		Standardized Coeficient	t.	Sig.
		B	Std-Error	Beta		
1	(Constant)	0.539	.490		6.610	.000
	Organizational operating synergy	0.729	.046	4.256	2.781	.001
	Bank size	0.692	.098	1.417	2.980	.001
	Risk diversification	0.539	.125	2.040	3.313	.000

It was observed that when independent variables were held constant (organizational operating synergy, bank size and risk diversification) to a constant zero, the financial performance of commercial banks in Kenya would be at 0.539 factor. A unit increase in organizational operating synergy would lead to a unit increase in the financial performance of commercial banks in Kenya by a factor of 0.729. A unit increase in bank size would lead to a unit increase in the financial performance of commercial banks in Kenya by a factor of 0.692. A unit increase in risk diversification would lead to a unit increase in the financial performance of commercial banks in Kenya by a factor of 0.539.

The resulting equation was;

$Y = 0.539 + 0.729X_1 + 0.692X_2 + 0.539X_3 + \varepsilon$

Y = Financial Performance

X_1 = Organizational operating synergy

X_2 = Bank size

X_3 = Risk diversification

The study established that organizational operating synergy as indicated by beta value (β= 4.256, $p < 0.05$), had a positive and significant impact on the financial performance of Kenyan commercial banks.. This agrees with Ingham, Kiran and Lovestam (2011) study that established the performance of mergers among top 500 firms not necessarily commercial banks and indicated that the period post-merger demonstrated a good performance for these firms. Furthermore, it was more likely where the integration of smaller firms into larger firms happened.

The study revealed that bank size as indicated by the beta value (= 1.417, p 0.05), had a positive and significant influence on the financial performance of Kenyan commercial banks. This concurs with Loderer and Martin (2010) who based their study on a total of 304 mergers using data collected on a 2o year period up to the year 1986 and indicated that the firms that had merged recorded significant improvement in size but did not perform better due to inefficiencies.

The study found that that risk diversification As indicated by beta value (= 2.040, p 0.05), had a positive and significant influence on the financial performance of Kenyan commercial banks. This is supported by the results of Muthiani's (2015) study, which used the opinions of the managers on whether the M & A conducted by GlaxoSmithKline Kenya PLC (GSK) had been significant on their performance. It was established that even despite the fact that organizational culture played a role in the process, the process enabled the firm to reduce its diversification risks. The M & A had aided in the long run improved performance.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This chapter contains a summary of the findings, conclusions, policy and practice recommendations, and suggestions for future research.

5.2 Summary

The study sought to determine how Kenyan banks' financial performance is affected by mergers and acquisitions. Merger and acquisition was evaluated in terms of organizational operating synergy, bank size and risk diversification and financial performance measure was ROA. Questionnaires were used to collect primary data, and data collection sheets were used to collect secondary data. The data was analyzed using descriptive and inferential statistics, and the results are presented below:

5.2.1 Organizational operating synergy

The purpose of the research was to determine the impact of organizational operating synergy as a result of merger and acquisition on the financial performance of Kenyan commercial banks. The study found that organizational performance has had a positive and significant impact on the financial performance of Kenyan commercial banks, as measured by beta value (= 4.256, p 0.05). A unit increase in organizational operating synergy would result in a factor of 0.729 increase in the financial performance of Kenyan commercial banks. The merger activity has improved the levels of growth, the merger activity has improved pricing power, the merger activity has improved the marketing power and that the merger activity has improved economies of scale.

5.2.2 Bank Size

The purpose of the study was to look into the effect of bank size on the financial performance of Kenyan commercial banks through merger and acquisition. The study discovered that bank size had a positive and significant influence on Kenyan commercial banks' financial performance, as measured by beta value (= 1.417, p 0.05). A unit increase in bank size would result in a factor of 0.692 improvement in Kenyan commercial banks' financial performance. The number of customers has increased after the merger, the company has made use of economies of scope to manage costs and that capital adequacy requirements has improved after the merger.

5.2.3 Risk Diversification

The study sought to assess the diversity of risk due to the integration and acquisition into the financial performance of Kenyan commercial banks. The study found that variance risk had a positive and significant impact on the financial performance of Kenyan commercial banks, as measured by beta value (= 2.040, p 0.05). Investment portfolio has increased after the merger because of the formation of new branches, as a result of acquisition and merger activity many branches have been established by our institution and that product portfolio has increased after the merger because of the formation of new branches.

5.3 Conclusions

5.3.1 Organizational operating synergy

According to the study, operation synergy has a significant impact on bank financial performance due to lower operating expenses, increased market share, consolidation of operations, and synergies within the banking industry. Banks' financial performance in

terms of profitability has improved. This has improved the bank's operational stability and effectiveness. Following a merger and acquisition, the bank's financing costs decreased, resulting in improved financial performance. In exchange, benefits might ascend in the short and medium term, while the bank's odds of long haul development and extension improve.

5.3.2 Bank Size

The study concludes that the increased bank size would result in efficiency gains that would be given to clients as higher store rates, lower loaning rates, and lower by and large revenue spreads. Be that as it may, expanding the size of a bank past specific limits presents diseconomies of scale, which prompts shortcoming. A bank's size increases the interest rate margins it enjoys. When compared to small banks, large banks have the opportunity to use their size to profit from lower financing costs because of economies of scale.

5.3.3 Risk Diversification

The study concludes that the diversification of a bank's operations varies depending on the bank. Diversification of risk is a risk-reduction technique that involves allocating investments across a variety of financial instruments. When banks diversify their risk, they lessen the measure of hazard they are presented to expand their profits. The objective of hazard broadening is to expand returns by putting resources into various regions that would respond contrastingly to a similar occasion. Diversification is a risk-mitigation strategy that allocates investment funds across different sectors in order to minimize risk and maximize returns.

5.4 Recommendations

5.4.1 Organizational operating synergy

The study recommends that Kenyan commercial banks ought to basically assess the blending foundations' general business and functional similarity and spotlight on catching long haul functional collaborations. They ought to widen their extension to fabricate high-performing supply chains with huge long haul potential gain that convey long haul worth to clients and partners. The study also recommends that the bank's management critically evaluate the merging bank's overall business and financial compatibility, with a focus on capturing long-term financial synergies.

5.4.2 Bank Size

The study recommends that there is a need for bank policies that place a higher priority on determining and monitoring their credit portfolio, client stores, and resource quality. The concentrate likewise proposes that all together for business banks to stay productive, they ought to have great portfolio the executives, which will support decision-production about speculation blend and strategy, coordinating with ventures to destinations, resource designation for people and establishments, and adjusting stores and credits against execution.

5.4.3 Risk Diversification

The study recommends that the banks should invest in a diverse range of assets, including bonds, stocks, and real estate etc so as to reduce the volatility and risk to their portfolio by holding investments that have a low correlation to one another. The commercial banks should distribute capital in a manner that diminishes openness to any one resource or

hazard, decreasing danger or unpredictability by putting resources into a different scope of resources.

5.5 Suggestions for Future Studies

The current study sought to determine how Kenyan banks' financial performance is affected by mergers and acquisitions. Merger and acquisition was evaluated in terms of organizational operating synergy, bank size and risk diversification and financial performance measure was ROA. As a result, the study recommends that additional research be conducted on other conceptualizations of merger and acquisition and financial performance. Furthermore, because the study context was commercial banks in Kenya, it is suggested that another study be conducted to focus on a different context.

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APPENDICES

Appendix 1: Introduction Letter

Dear Respondent,

I am conducting an important study on mergers and acquisitions as well as the financial performance of Kenyan commercial banks. This is in fulfillment of award of the Kenyatta University Master of Business Administration (Finance Option) degree.

Please complete the attached questionnaire with your own genuine agreement to each question. There are no incorrect answers to any of these statements. This is scholarly work, and your obscurity is completely authorized; your name won't show up anyplace in the report.

Kindly spare some of your time and respond to the questionnaire.

Thank you very much in advance,

Sincere Regard

Maureen Mutuku

Appendix II: Questionnaire

SECTION A: BASIC INFORMATION

1. **Work Experience**

a) Below 3 Years ☐
b) 4 – 7 Years ☐
c) More than 7 Years ☐

2. **Department**

a) HR ☐
b) IT ☐
c) Finance ☐
d) Marketing ☐
e) Operations ☐
f) Administration ☐
g) Retail Banking ☐

3. How many employees are in your organization?

a) 1 to 10 employees ☐
b) 11 to 50 employees ☐
c) Over 50 employees ☐

Section B: Organizational Operating Synergy

Please mark (x) in the box which best describes your disagreement or agreement

No	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
1.	The merger activity has improved economies of scale					
2.	The merger activity has improved economies of scope					
3.	The merger activity has					

	improved pricing power					
4.	The merger activity has improved the marketing power					
5.	The merger activity has improved the levels of growth					

Section C: Bank Size

This section establishes how the financial performance of merged institutions is affected by bank size. Please mark (x) to describe your disagreement or agreement to the statements below.

No	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
1.	The company has made use of economies of scope to manage costs					
2.	The company has made use of economies of scale to manage costs					
3.	As a result of acquisition and merger activity many branches have been established by our institution					
4.	The number of customers has increased after the merger					
5.	Capital adequacy requirements has improved after the merger					

Section D: Risk Diversification

This subsection assesses how the merged institutions' financial performance is affected by risk diversification. Please mark (x) what best describes your agreement or disagreement.

No	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
1.	As a result of acquisition and merger activity many branches have been established by our institution					
2.	New branches established after the merger have resulted into the expansion market portfolio					
3.	Product portfolio has increased after the merger because of the formation of new branches					
4.	Investment portfolio has increased after the merger because of the formation of new branches					
5.	New branches established after the merger has attracted a wide human resource portfolio					

Appendix III: Secondary Data Collection Template

Year	ROE
2018	
2017	
2016	
2015	
2014	