

EFFECTS OF CAPITAL BASE ON SHAREHOLDERS' WEALTH OF KENYAN LISTED COMPANIES INVOLVED IN MERGERS AND ACQUISITIONS

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Abstract

The study sought to establish the effect of capital base on the shareholders' wealth of Kenyan listed firms involved in Mergers and Acquisitions (M&A). The study adopted a descriptive research design. Comparisons were made between the mean of 3 years pre-merger/acquisition and 3 years post-merger/acquisition financial ratio while the year of merging and period of acquisition were exempted. The study found that the performance of the Kenyan companies in shareholders wealth was on average the same following the M&A. In addition, performance in capital base was on average the same before and after M&A. Furthermore, the study established that an increase in capital base will lead to a significant increase in shareholders' wealth. The study recommends that management should not only undertake M&A in order to improve operation and sustain failing businesses but also improve their competitiveness and financial standing. In addition, management should come up with a sound strategy towards asset and liability management so as to avert the problem of mismatching investments and also the quality of assets should be enhanced. Management should put into consideration the degree of transferability and marketability of assets invested in so that the assets can provide liquidity to the firm with ease.

Keywords: Capital base, mergers and acquisitions, shareholders wealth, listed companies

INTRODUCTION

Corporations carry out numerous ways in efforts to boost money performance that is predominant to the success of any organization. It reflects the money health of firms within the market and also the performance as compared to alternative players within the trade. Mergers and Acquisitions are undertaken in efforts to boost organization's performance thanks to the advantages they're believed to hold on. Management considers Mergers and Acquisitions to cut back prices and expenses and maximize shareowner price (Maranga, 2010). Failure by the management to undertake financial investments which are risky that may otherwise be needed to maximize wealth of shareholders, however, poses a conflict of interest between shareholders and management (Clacher, Hillier, & Mccolgan, 2010).

Whether getting company shareholders expertise a wealth impact from Mergers and Acquisitions could be a matter of in progress discussion among educational researchers (Hassan, Patro, Tuckman, & Wang, 2007; Nyambura, 2014). Mergers and Acquisitions can potentially improve cost efficiency by increasing scale efficiency, scope efficiency or managerial efficiency. Maranga (2010) indicated that firm which engaged in take-over of subsidiaries had no significant changes in levels of their cost efficiency after mergers. However, some of the firms that merged with other banking institutions demonstrated significant declines in their cost efficiency. Sufian (2004) found that in Malaysia the bank's post-merger average overall efficiency of 89.1% was still lower compared to pre-merger when the bank had been operating at about 95.8% average overall efficiency, as the merged entity is burdened with high overhead costs and excess employees.

An organizations capital is finance ascribed to the investors (Proprietors) as distributed in a critical position sheet and for the most part is required to help business. Sufficient capital is the quantum of assets which an organization ought to have or plan to keep up to direct its business in a judicious way (Olalekan & Adeyinka, 2013). The more the capital an organization has, the more misfortunes it can support without going bankrupt, therefore, capital gives the measure to the time a firm needs to redress for pass, for example, inward shortcoming or negative improvements.

Capital sufficiency looked at for a long time pre and post-merger from the money related proclamations of the example organizations by Lole (2012) derived that the budgetary execution of Faysal bank constrained reductions inconsequential as far as capital amplenness measures. As per Gachanja (2013) the respondents concurred that the capital base of greater part of the banks expanded after securing or consolidating and accordingly the business banks could meet the center capital prerequisite by the national bank. Also, taking all the autonomous factors at zero, at that point a unit increment in capital base prompted 0.642 increments in execution,

delineating that capital base keeps on having the main impact on business banks execution. Consequently capital base was huge in clarifying the connection amongst Mergers and Acquisitions methodology and the execution of business banks in Kenya since their levels of noteworthiness are underneath 0.05.

In Kenya Mergers and Acquisitions occurs in different sectors in the economy. The study is undertaken involving seven listed companies involved in Mergers and Acquisitions across six different sectors in Kenyan for the period between the years 2008 and 2014. The different sectors were agriculture, manufacturing, petroleum, banking, mining, communications and technology. In each of the sectors only one firm was selected save for petroleum sector. The firms selected included Rea Vipingo, Unilever, Total Kenya, KenolKobil, Stanbic holdings, Bamburi cement, and Safaricom Ltd. The enlisted firms were involved in M&As in the respective years as follows. Rea Vipingo (2014), Unilever (2009-2010), Total Kenya (2007-2009), KenolKobil (2008), Stanbic holdings (2008), Bamburi cement (2014), and Safaricom Ltd (2008-2009).

LITERATURE REVIEW

The relevant theory reviewed for this study was the User Cost of Capital Theory. It argues that the capital utilized by firms is leased however not possessed by the organizations that utilization it along these lines firms must think about this hypothesis before getting into a Mergers or Acquisitions relationship (Creedy & Gemmell, 2015). For firms to obtain different others or consolidation, a firm should think about the hypothesis in settling on its choice. That is, to keep utilizing its own particular capital, team up with another firm in utilizing it or offer it. The impediments of this hypothesis is that it doesn't make sense of any system through which desires influence the adjustment in capital and it doesn't provide food for the change of cost of capital. This theory is relevant in this study in that shareholders are entitled to dividends from the capital base at the end of each financial year and should appreciate seeing the value of their shares going up.

Different studies on corporate Mergers and Acquisitions have concentrated on the impact of Mergers and Acquisitions on firm execution. This is on account of mergers and acquisitions have been the commonest technique for corporate procedure to enhance firm execution. Various investigations on mergers have uncovered differing discoveries and conclusions. For instance Kiplagat (2006) looked into on the impacts of mergers on money related execution of organizations recorded at the Nairobi Security Exchange (NSE). The populace utilized as a part of the examination was 48 organizations recorded on the Nairobi Stock Exchange and an example of 20 recorded organizations was reached. It comprised of 10

organizations that blended and 10 that never combined and were constantly in activity for the period partners were consolidated.

Selvam, Babu, Indhumathi, and Ebenezer (2009) conducted a study on the impact of mergers on the corporate performance of acquirer and target companies in India. A sample of companies which underwent merger in the same industry during the period of 2002-2005 listed on the Bombay Stock Exchange was used. The study focused on comparing the liquidity performance of the thirteen sample acquired and target companies before and after the period of mergers by using ratio analysis and t-test. It was found out that the shareholders of the acquirer companies increased their liquidity performance after the merger event. Chesang (2002) studied how merged commercial banks in Kenya influence their financial performance.

Chesang found that firm size and financial performance of acquiring firms can be the determinants of poor performance in the post-acquisition period. Muya (2006) carried out a survey of experiences of mergers and found that mergers do not add significant value to the merging firms. Njenga (2004) also conducted a survey on investigation into whether the demerger of coffee marketing societies have created or eroded owners' wealth in parts of Central Kenya. Njenga found mixed results on whether demergers leads to wealth creation or erosion of coffee firms as depicted by both positive and negative returns on post-merger firms.

Njoroge (2007) led a review of Mergers and Acquisitions encounters by budgetary foundations in Kenya. The investigation of the money related foundations execution for pre and present merger periods sort on set up whether there was noteworthy change of budgetary execution on regions of benefit, venture and liquidity. The aftereffects of the information dissected demonstrated that Return on Asset and Return on Investment show a unimportant distinction while Return on Equity and Debt Equity Ratio show huge contrast between measures of execution when merger.

Ndung'u (2011) looked to decide the impacts of Mergers and Acquisitions on the budgetary execution of business banks in Kenya. The examination concentrated on the monetary execution of 24 business banks in Kenya which converged somewhere in the range of 1999 and 2005. Relative examination of the bank's execution pre and post-merger periods was directed to build up whether mergers prompt enhanced budgetary execution. He presumed that there was change in budgetary execution after banks combined. The examination additionally found that there was general increment in the benefit of the banks after merger and furthermore increment in dissolvability and capital sufficiency.

RESEARCH METHOD

This study used descriptive survey design to depict whether Mergers and Acquisitions do have an effect on the shareholders wealth of Kenyan listed companies involved. The target population of this study comprised of the Kenyan listed companies that engaged in Mergers and Acquisitions for the period between the years 2008 and 2014. The rationale for selecting data between the years 2008 and 2014 is that there was consistence of facts and figures as a result of published reports on mergers and acquisitions. Comparison was made between the mean of three (3) years pre- and three (3) years post-Mergers and Acquisitions while the year of acquiring or merging was exempted. The study used secondary data on financial statements of the merged companies before and after the M&As. The fundamental or intrinsic value was compared before and after the M&As. Secondary data was obtained from the Nairobi Securities Exchange and the Capital Markets Authority (CMA) annual reports. Data from financial statements included; total assets, equity, operating revenue, operating revenue, net profit after tax and number of shares. Data from securities exchange included net revenue of firms listed in the Nairobi Securities Exchange and that had engaged in Mergers and Acquisitions. The collected data was presented through frequency tables and various measures of central tendency such as means. The researcher conducted two-sample t-tests to ascertain and compare the mean performance of each of the variables before and after Mergers and Acquisitions. Afterwards multivariate regression analysis was used to establish the effect of the three factors on shareholders wealth.

ANALYSIS AND RESULTS

Descriptive analysis technique was utilized which involved use of descriptive statistics and tabulations. The summary statistics for the firms in Kenya before and after the Mergers and Acquisitions are given in Table 1.

Table 1: Summary Statistics Before and After M&A

Variable	Before M&A				After M&A			
	Earnings per share	Capital base	Cost efficiency	Market share	Earnings per share	Capital base	Cost efficiency	Market share
Mean	5.15	0.45	1.49	0.26	6	0.51	2.19	0.26
Std. Dev.	4.04	0.21	0.98	0.23	8.41	0.33	2.73	0.23

The mean earnings per share before the M&A was 5.15 while after the M&A, EPS was 6.00 hence, the EPS increased following the M&A, in line to findings by Mboroto (2013) who

established there was an improvement in the firm's performance after the M&A takes place. Similarly, the capital base before and after M&A was on average 0.45 and 0.51 respectively, showing the capital base increased following the M&A.

Table 1 further illustrates that cost efficiency before and after M&A was 1.49 and 2.19 respectively, showing that there was an increased CE as a result of M&A, disagreeing with those in a Malaysian study by Sufian (2004) that the bank's post-merger average overall efficiency was still lower compared to pre-merger average overall efficiency and also by Maranga (2010) that merged firms demonstrated declines in their cost efficiency. The market share before and after M&A was on average 0.26 and 0.26 respectively, indicating the market share did not change following the M&A. This negated deductions by Avulala (2015) that mergers and acquisition of companies in the insurance industry have led to increased market share of the merged/acquired companies and also Ondieki and Njangiru (2015) that merging their business enlarged the bank's market share.

Both the dependent variable and the three independent variables were further subjected to two-sample test to ascertain the difference in the mean performance before and after the M&A and its significance level as shown in table 2.

Table 2: Two-Sample T-Tests for All Variables

Variable name and T-statistics	Capital base			
	EPS	(CA)	CE	Market share
Difference	-0.85	-0.06	-0.70	-0.001
(T-statistics, P-value)	(0.4155 0.3400)	(0.6868 0.2481)	(1.0957 0.1399)	(0.015 0.9881)
Mean Before M&A	5.15	0.45	1.49	0.2636
Mean After M&A	6.00	0.51	2.19	0.2647

The table 2 shows that the difference between the mean performance of EPS before and after the M&A was -0.85 and it was not statistically significant at 5 percent level. This clearly indicates that the firms' performance of EPS was the same before the M&A as its performance after the M&A. These findings concurs with those established by Mboroto (2013) who revealed that there was an improvement in the firm's performance after the M & A takes place.

The difference in capital base (CA) and CE before and after the M&A was respectively - 0.06 and -0.70, indicating an improvement in CA and CE following M&A. This difference was not statistically significant implying that, the performance of the firms in capital base and cost efficiency was on average the same before and after M&A. The findings are in line with those by

Lole (2012) who deduced that the financial performance of Faysal bank limited was insignificant in terms of capital adequacy measures. Hence, capital base and cost efficiency was not affected by the M&A.

Table 2 further shows that the difference in market share before and after the M&A was -0.001, indicating an improvement in market share following M&A. This difference was not statistically significant indicating that, the mean performance of the firms involved in market share increased but statistically was the same after the M&A compared to its average before the M&A, similar to findings by Ondieki and Njangiru (2015) that the process of merging enlarged the bank's market share.

Regression analysis

The researcher sought to establish the effect of capital base on shareholders wealth of listed companies involved in M&A.

Table 3: Regression Model

Random-effects GLS regression	Model
Explanatory variables	Coefficient (P-Value)
Capital base	14.5844* (0.000)
Cost efficiency	-0.4715 (0.222)
Market share	-2.7023(0.697)
Constant	0.1857 (0.948)
R-squared: Within	0.2629
Between	0.6492
Overall	0.5041
Chi-square statistic	19.22* (0.0002)

Upon controlling for other independent variables a positive coefficient of 14.197 on capital base was realized with a p-value of 0.000 which was statistically significant at the 0.05 level. Hence failing to reject that, capital base has no effect on shareholders wealth. This indicates that, capital base is positively associated with shareholders wealth, and it does have a statistically significant effect on shareholders wealth.

The findings above implies that as capital base increase this will lead to an increment in EPS and the increment in EPS following an increment in capital base will be large to guarantee a significant change in the shareholders wealth. The findings are in line with those in a study by Onikoyi and Awolusi (2014) who established that there is significant relationship between shareholders wealth and capital base of the merged banks. In addition, it concurs with the findings by Gachanja (2013) who established that capital base was significant in explaining the relationship between Mergers and Acquisitions strategy and the performance of commercial banks in Kenya.

The R^2 values indicate that, 26.29% of the variations in shareholders wealth, as measured by earnings per share, within the firms are explained jointly by capital base, cost efficiency and market share. 64.92% of the variations in shareholders wealth between the firms are explained jointly by capital base, cost efficiency and market share. Only 50.41% of the variations in shareholders wealth of the firms involved in M&A (considering panel data) are jointly used to predict the level of shareholders wealth.

The joint effect of all the variables included in the model produced a chi-square statistic of 19.22 with an associated p-value of 0.0002. Since the p-value did not exceed 0.05 levels, consequently we reject the hypothesis with the indication that capital base, cost efficiency and market share do have a statistically significant joint effect on shareholders wealth. Therefore all the coefficients of the explanatory variables integrated in table 3 were significantly different from 0.

CONCLUSIONS AND RECOMMENDATIONS

Based on the findings of the study, it was concluded that the performance of the firms in shareholders' wealth, capital base and cost efficiency and market share was on average the same after the M&A compared to its performance before the M&A. An increase in capital base will lead to an increase in EPS large enough to guarantee a significant change in the shareholders' wealth. However, an increase in either cost efficiency or market share will lead to a reduction in EPS, though not large enough to guarantee a significant change in the shareholders wealth.

Emanating from the aforementioned conclusions the study recommends the following:- Management ought not just to embrace Mergers and Acquisitions keeping in mind the end goal to enhance task and maintain falling flat organizations yet additionally enhance their aggressiveness and money related standing. Further management should concoct a sound system towards resource and obligation administration in order to turn away the issue of confounding ventures and furthermore the nature of advantages ought to be upgraded. Also

management should put into thought the level of transferability and attractiveness of benefits put resources into so these advantages can furnish liquidity to the firm easily.

In future, a comparative analysis shall be conducted to ascertain the effect of Mergers and Acquisitions in the different sectors of the economy. Also future studies need to be conducted using other variables related to shareholders' wealth. Finally Studies need to be conducted on the determinants of shareholders' wealth for a longer period of time.

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