

INFLUENCE OF THREAT OF NEW ENTRANTS ON PERFORMANCE OF OIL INDUSTRY IN SOUTH SUDAN

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Abstract: The purpose of this study was to examine the influence of threat of new entrants on performance of oil industry in South Sudan. The specific research question guiding the study was: What level of influence does threat of new entrants have on performance of oil industry in South Sudan? The research design used was descriptive research and analytic research; descriptive research described the phenomena of oil industry performance while analytic design established relationship among these phenomena. Of the 84 self-administered questionnaires distributed to the middle and top management of all oil firms operating in South Sudan, 66 were filled and returned representing a 78.6% response rate. The study found out, threat of new entrants have positive significant influence on performance of oil industry in South Sudan and recommends: the government of South Sudan to develop or update existing policies and regulation of the oil industry in South Sudan based threat of new entrants; oil firms in South Sudan should consider influence of new entrants to their business; lastly, oil firms preparing to enter South Sudan oil fields should review

Keywords: new entrants, performance, oil industry, South Sudan.

1. INTRODUCTION

Different organizations have implemented different internal strategies as a control mechanism on factors that influence performance such as strategic coherence, performance management style, social norms and how they influence behavior, standards at work, communication, supportive supervision, leadership functions, resources, work ethics, structures and work culture. However, strategies for developing and emerging economies face unique challenges and as a result, the assumptions that internal strategies for developed countries will work in developing ones need to be challenged through empirical research. Arguably, markets in developing countries, provide a new context in which to understand issues of strategy, competition and institutions among others (Hough et al., 2008). Strategy scholars such as Khanna et al. (2005) and Wright et al. (2005) appear to agree that strategies for emerging markets face unique challenges, and that what works in the developed nations is likely not to work in other contexts and especially those of developing nations.

According to Hough, et al. (2008), research on the practice of organization strategic management in emerging economies has grown and coverage of countries and regions in emerging economies has been uneven. South America has had a large share of the research based on different models and theories which clearly depicts strategies used in business. Similar studies are required for new and developing markets as observed by Wright et al. (2005) as quoted in Hough, et al. (2008).

Oil industry in Africa is growing. In 2013, Africa produced nearly nine million barrels of crude oil per day with more than 84% from Nigeria, Libya, Algeria, Egypt and Angola. According to 32 National Oil Companies (NOC) in Africa, more international companies are increasingly investing in the oil industry in Africa with Sonangol (Angola), Sonatrach

(Algeria), Statoil (Norway), ONGC (India), PetroSA (Ghana), CNPC and Sinopec (China), Statoil, Gazprom (Russia) and CNOOC (China) eyeing Tanzanian. (PWC, 2014; African Development Bank and Africa Union, 2009). This trend is similar to the global trend as the multinationals are involved in extraction, transportation and wholesale hence creating a monopoly in the oil industry which lowers performance of the industry (Porter, 2008). Further, African government implements new policies that attempt to increase their share in proceeds thus increasing rivalry between government, investing firms and new entrants (PWC, 2013).

However, different studies show that oil industry is capital intensive businesses especially on oil extraction and refining which limits the number of new entrants in the industry. Despite this, PWC (2012) study revealed most African governments are also a source of barriers for new entrants with strict rules on the license for operation, legal requirement, availability of infrastructure and environmental factors. This forces most oil and gas companies to contract local companies, procure local suppliers and labor, most of whom lack required knowledge (PWC, 2014; Brown, 2013). The oil firm that enters such markets dominates as others are limited to entry which lowers the performance of oil industries in comparison to free market economy.

According to BP, (2014), Brown, (2013) and PWC (2013), the shortage of trained oil and gas workers is a concern globally. PWC (2013) further urges donors like the World Bank to invest in capacity building which in turn will prevent suppliers' monopoly due to lack of professional labor required for production. This will lead to expansion on partnership, transportation, refinery and distribution. Such a partnership is the one signed between Kenya and South Sudan in January 2012 'to build a port to the Kenyan city of Lamu and sought in February 2012 to strike a deal with Ethiopia to build a pipeline via Ethiopia to Djibouti's port' (Brown, 2013; P. 858).

In micro-economics, the forces of demand and supply determine the cost of goods and services which determines the profit level in a normal competitive environment. However, the possibility of new firms entering an industry may affect competition and profit. For example, in a monopoly market, the performance is poor due to lack of competition in comparison to free market where entry is determined by the market forces. Porter sum up the threat to entry as follows:

'Barriers to entry are more than the normal equilibrium adjustments that markets typically make. For example, when industry profits increase, we would expect additional firms to enter the market to take advantage of the high profit level, over time driving down profits for all firms in the industry. When profits decrease, we would expect some firms to exit the market thus restoring market equilibrium. Falling prices, or the expectation that future prices will fall, deters rivals from entering a market. Firms also may be reluctant to enter markets that are extremely uncertain, especially if entering involves expensive start-up costs' (Porter, Lorsch, and Nohria, 2004, p63).

South Sudan independence came with occupation of 75% of oil reserve of Sudan. According to Africa Business initiative (2011), South Sudan sits on the third-largest oil reserves in Africa, with 98% of the government's revenue and GDP from oil production. However, with lack of resources, South Sudan remains dependent on the north for processing, refinement, and export despite challenges that have hindered production such as war and competent human capital (Africa Business Initiative, 2011; Brown, 2013; PWC, 2014).

2. LITERATURE REVIEW

According to Porter (2008), the threat of entrant into an industry depends on the barriers to entry that are present, coupled with the reaction from the existing competitors in the industry that the new entrant can expect to meet. If barriers are high and existing companies given a sharp retaliation, the threat of entry is low. High barriers diminish the competitive advantage the new entrants could pose. Porter further outlined high threat of entry means competitors are likely to be attracted to enter into the market due to high profit they are likely to enjoy. This creates a platform where companies are likely to enter with ease which decreases the market share and profitability of existing competitors. In the long run, this may lead to change in existing product quality or price level for firm sustainability due to competition.

High threat of entrants affects the competitive environment for oil firms already in the market. The high threat increases competitors which in turn influences the existing firms' performance through profitability, market share, and efficiency. The increase in number of industry increases competition of the same market and resources. On the other hand, low threat of entry makes an industry less competitive and the possibility to increase its profit level especially in a growing market due to expansion (Lopez-Claros et al., 2008; Porter, 2008).

International Journal of Novel Research in Marketing Management and EconomicsVol. 3, Issue 2, pp: (157-164), Month: May - August 2016, Available at: www.noveltyjournals.com

Economies of scale are a key factor in the oil industry which affects oil industry performance. According to Sahu and Parekh (2012), oil and gas industry depends on economies of scale due to its commercial viability and feasibility of projects. Such economies of scale helps companies to achieve competitive advantage through high market share, due to cost optimization, time reduction and commercial viability of a project. Firms with high economies of scale are likely to have a high market share in production, exploration or transportation. With high market share, the firms are likely to leave a monopoly hence high profit level and profitability (Porter, 2008). Despite this, the internal process and customer satisfaction differ with the firms market share; with monopoly, the buyers have lower power hence the satisfaction has minimal significance similar to the firms internal processes.

Similar to economies of scale, a number of research found out, new entrants to the extraction and refining industry is highly capital intensive. This has minimized the number of refineries to one or two in smaller EU member states (Grünig and Best, 2007). Further, the high capital intensive aspect has been attributed to specialized labor required at different stages of processing, and intensive equipment due to intense processes and procedure at different stages. Industries involved in the business have only been made stronger as research shows due to the capital intensive. Due to this, multinational companies have evolved and largely been involved in extraction, transport, refinement to wholesalers and retail trade due to what Porter (2008) attributed to economies of scale. Similar to the economies of scale, the cost of entry affects performance by increase in profit due to monopoly which directly increases the market share but indirectly affects the customer satisfaction and internal processes of the industries.

Sahu and Parekh (2012) and Porter (2008) posit it that the market shares can be determined by time of entry or the duration that one has been operating in an industry. The duration of operation determines the market share based on economies of scale and area of operation. If the area of operation allows a firm to expand, it captures more market share over a period of time based on the economic competitions. Such companies are in many countries and in some is a complete monopoly (BP, 2014). Examples of such companies are ExxonMobil, Royal Dutch Shell or BP, Total, TexacoChevron or TotalFinaElf (Grünig and Best, 2007).

Based on the above, duration of operation can affect the profit level and firm growth in the market share based on their growth strategy and business structure (Sahu, and Parekh, 2012). However, this may not directly impact customer satisfaction and efficiency level/internal business process especially if the firm has monopoly power which affects the buyers' power in the market (Porter, 2008).

Technology has evolved over time and the required technology for operation of the oil industry is key for its performance. According to Grünig and Best (2007) and Lopez-Claros *et al.*, (2008), technology in oil industry is key in reducing the capital for investment, economies of scale, it ensure quality oil products, and saves costs in exploration. Without appropriate technology, high loss can be experienced in the oil industry. Technology is key for functions such as converting natural gas and coal to liquid fuel, minimize pipeline failure, remote monitoring, visualization, security, environmental monitoring (SRI, international, 2015). Technology can lead to invention which increases the profit level, market share, customer satisfaction of an oil firm due to quality produce and efficiency of the oil industry. This is also supported by David (2009), Ehlers and Lazenby (2010) who stated that price, quality and innovation as a strategy determines the growth in market share hence increase in profit in the long run.

Although emerging studies identify the opportunity in oil recycling, new entrants can capitalize on this existing gaps in most countries if they focus on provision of incidental services. However, Porter (2008) and PWC (2012) support Grünig and Best (2007) through in the phase of mergers and acquisitions with intend to build market position that can cause major shake-ups. The limitation of such is only the companies as can expand to exploration or incidental of oil industry services. Further, PWC (2012) study on Gas in South Africa revealed, legal regulatory environment were not supportive of new entrants despite the attractiveness of the deal to investors. Also, the capital requirement and lack of infrastructure required to start gas production was pointed out as a significant threat to new entrants. With the gas production process being similar to oil, or as a substitute of oil in some commodities, the threat of new entrants in gas industry can be perceived as similar in oil industry. It is also important to note, threats to new entrants encourage speculative approach to market entry which in the long run is harmful to the development of the industry to all the stakeholders; industry, investors and government.

International Journal of Novel Research in Marketing Management and EconomicsVol. 3, Issue 2, pp: (157-164), Month: May - August 2016, Available at: www.noveltyjournals.com

Whenever new firms easily enter a particular industry the intensity of competitiveness increases as the market remains the same. Such new entrants can threaten the market share of existing competitors by bringing additional production capacity to the industry (David, 2009). The threat of entry is a force therefore that refers to the possibility that profits of established companies in the industry may be reduced by the entrants of new competitor organizations (David, 2009; Ehlers and Lazenby, 2010; Pearce & Robinson, 2011; Porter, 2008). These findings are in line with Porter's factors on threat of new entrants: Economies of scale, product differentiation, capital requirements, switching costs, access to distribution channels and Government Policy (Lopez-Claros et al., 2008; Porter, 2013; PWC, 2012; 2014). Another study by PWC in 2014 on Africa titled 'On the Brink of a Boom Africa Oil & Gas Review' showed that, South Sudan has an investment promotional act which provides incentive to the community and investor. Investors are given capital allowance of 20% to 100%, deductible annual allowance of 20% to 40%, and depreciation allowance of 8% to 10%. In return, investors in the oil industry are required to construct infrastructure such as roads, schools and hospitals in their area of operation. The impact of such encouragement by the government to the new entrants remains unknown and is further explored in this study.

Economies of scale are achieved when production is increased during a given period, and this results in lower production costs because of the spreading of costs over a larger number of units (Ehlers and Lazenby, 2010). This means that the per unit cost of production becomes lower and lower over time. Companies enjoying economies of scale can afford to keep prices constant and increase profits. Sometimes they can lower their prices to a point where other companies cannot match. Economies of scale can also arise from effectiveness and efficiency in distribution, utilization of sales force or even technology, financing and from other functions of business (David, 2009). New entrants do not usually have the advantage of economies of scale. However, companies diversifying through acquisition into an industry from other markets with intent to build market position can cause major shake-ups (Porter, 2008; PWC, 2012). They should also be viewed as new entrants.

Product differentiation relates to the belief by customers that a company offers a unique product. Customers' perception is that the product is different from competing products and close substitutes. The customers are loyal to the organization and do not easily shift their loyalty (Pearce & Robinson, 2011). Product differentiation means that established organizations have brand identification and customer loyalties, which stem from past advertising, customer service, product differences, or simply being the first in the industry and benefiting from first movers advantage (Pearce & Robinson, 2011; Porter, Lorsch, and Nohria, 2004; Ehlers and Lazenby, 2010). New entrants have to spend heavily to overcome existing customer loyalties. The process is likely to take a long time.

New entrants require considerable resources to compete in a new industry. Capital is required to buy physical facilities, production facilities, inventories, to meet start-up costs, to carry out marketing activities, and to bridge customer credit among other costs (Ehlers and Lazenby, 2010). The need to spend huge capital resources in order to compete in a new industry creates a barrier to entry. Sometimes there may be need to spend resources on risky or unrecoverable up-front advertising or research and development. These are barriers to entry for new comers and can be discouraging in themselves. Even if capital is available on the capital markets, entry represents a risky use of that capital. Existing or going firms have a cushion or advantage in this regard (Porter, Lorsch, and Nohria, 2004).

Switching Costs are once-off costs which customers incur when they switch from one supplier's product or service to another (David, 2009; Ehlers and Lazenby, 2010). Switching costs create a barrier to entry. Switching costs may include employee retraining costs, cost of new ancillary equipment, cost and time in testing or qualifying a new source, product redesign, or even psychic costs of severing a relationship (Porter, Lorsch, and Nohria, 2004). New entrants can overcome these high switching costs by offering either a substantially lower price or a much better product or service to attract customers. This engenders improvements in cost or performance, is an expensive affair.

Access to distribution channels is important as new entrants must get their products to customers. New entrants have to create their own distribution channels for a product, especially where wholesale and retail channels are limited, or have to persuade distributors to carry their products (Ehlers and Lazenby, 2010). Existing competitors may have close ties with channels based on long term relationships, high quality service, exclusive relationships and even some form of control. This creates a high barrier that is not easy to overcome. When this is the case the option is usually to create own distribution channel. Creating own channels of distribution is expensive and takes a long time. In most cases, new entrants have to convince existing distributors to carry their products through price breaks, cooperative advertising allowances and other benefits, all of which reduce profits (Porter, 2008).

Cost Disadvantages independent of Scale arise from the fact that established firms in an industry may have cost advantages independent of their size or economies of scale, that are not easily replicable by potential entrants. These cost advantages may include favorable access to raw materials, favorable locations, Government subsidies, proprietary product technology (product know-how or design characteristics) kept proprietary through patents or secrecy, and favourable effects arising from learning or experience curve. As a result of learning or experience, there is an observed tendency for unit costs to decline as the firm gains more cumulative experience in producing a product (Porter, 2004; Ehlers and Lazenby, 2010). It may be difficult for new entrants to duplicate these cost advantages enjoyed by incumbent firms. Reducing the relevance of these advantages by new entrants may be a difficult and expensive undertaking.

Government Policy is a major source of entry barriers. Government can limit or even foreclose entry into industries through such control mechanisms as licensing requirements and limits to access to raw materials (Porter, 2008). Other government controls may include requirements for standards for goods and services and also regulations that may affect industries e.g. liquor retailing, trucking, banking, and railroads (PWC, 2014).

3. METHODOLOGY

This study employed the two approaches of design; descriptive and analytic research. Descriptive research aims at describing phenomena or narrating how various behavior and events occur. On the other hand, the analytic research seeks to establish relationships among phenomena or variables by asking “what” and “why” certain behaviors occur and “how” these behaviors relate to other types of behaviors and other variables.

Using census method, all 21 oil firms operating in South Sudan constituted the population of study. These companies were identified physically and counter checked with the Chamber of Commerce and Industry for authenticity. All the middle and top managers of these companies were involved in the survey. Before data collection, pre-test was conducted for validity and reliability test. Reliability refers to the consistency and stability of scores obtained from an instrument, (Creswell, 2005; Kothari, 2003). Structured questionnaire was used to obtain information with Cronbach’s reliability alpha shows an internal consistency of .858 (85.8%) which is highly reliable. Of the 84 self-administered questionnaires distributed to the middle and top management of all oil firms operating in South Sudan, 66 were filled and returned representing a 78.6% response rate.

Cleaned data was analyzed thematically using multi-linear regression modeling. According to Kothari, (2003), Multi-linear model identifies relationship of variables based on clustered dependent variables. Basic descriptive analysis was performed for demographic data and beginning data followed by correlation to identify background and new entrants relationship. Lastly, Regression tested the magnitude of change of oil performance in relation to new entrants.

The regression model used was:

$$\text{Performance} = \beta_0 + \beta_1 \times \text{Threat of new entrants} + \varepsilon$$

4. FINDINGS

Background Information:

Correlation between age and management level shows a positive correlation ($P=.005$, $r=.345$) indicating as one advances in age the likelihood of advancing from middle management to top management because of his/her age is 11.9% (r^2 of .119). Similarly, there is positive correlation between management position and duration that one has served in the company ($P=.0001$, $r=.534$) indicating 28.5% (r^2 of .285) likelihood of one ascending from middle management to top management based on the year of service in an oil company operating in South Sudan.

When respondents were asked to state the ownership of the firm where they work as either government, internationally owned, joint venture or locally owned; 36.4% were government owned followed by 25.8% that were internationally owned, 21.2% as joint venture and 16.7% were locally owned. Being a multi-response question, 46.0% of firms were involved in more than one type of oil business and 54% concentrated in only one type of business as follows; 27.0% were in oil mining, 11.1% in oil processor, 9.5% in oil distributor and the least business type was oil waste management and oil piping evenly at 3.2% each. This indicates nearly half of the oil companies in South Sudan are involved in more than one type of oil business.

Threat of New Entrants:

Threat of new entrants on Porter's five forces of industrial competition discussed in this research were: economies of scale determines market share of a firm; market share is determined by the time of entry or the duration that one has been operating; the cost of entry determines the profit of a firm; the economy of scale determines the profit of a firm; and the technology required for operation can prevent a firm from operation.

On the general perception on effect of threat of new entrants on performance, there was general agreement as follow: Economies of scale determine profit at 87.9%, skewness of -1.428; Operation technology required can prevent a firm from operation at 84.4%, skewness of -1.461; Cost of entry determines the profit of a firm at 81.8%, skewness of -1.291; Economies of scale determine market share at 86.2%, skewness of -1.031; and time entry/duration of operation at 77.2%, skewness of -.627. Only time of entry/duration of operation was moderately skewed ($-.627 < 1$). Similarly, comparison by mean shows economies of scale determine profit had the highest $M= 4.23$, $SD = .837$; followed by operation technology required can prevent a firm from operation at $M= 4.06$, $SD = .875$; cost of entry determines the profit of a firm $M=3.98$, $SD=.953$; economies of scale determine market share $M=3.98$, $SD=.712$; and duration of operation at $M=3.95$, $SD =.812$. Though the variance of SD was not sequential as mean, the mean had similarity with skewness which supports, the respondents 'agreed' on the general perception on threat of new entrants.

Type of Business and Threat of New Entrants:

Comparison of the mean of type of business based on the threat on new entrants reveals: in economies of scale determine market share, economies of scale determine profit and operation technology required can prevent a firm from operation, oil waste management had the highest mean ($M=5$) and oil piping with the lowest mean ($M=2.0$). This shows oil waste management depends on the economies of scale and operation technology to capture the market share and make profit unlike oil piping which has minimal effect on the economies of scale and profit.

A comparison between the type of business that the firms are involved in and threat of new entrant using non-parametric equation show a positive correlation between type of business and whether economies of scale determines the market share, $p=.0005$, $X^2 = 53.108$, $df (15)$. This means, economies of scale determines the market share of oil firms in South Sudan regardless of the type of business that a firm is involved in.

On the relationship between the type of business and whether market share is determined by time of entry or the duration that one has been operating, there was a positive relationship, $p=.004$, chi-square (X^2) of 33.257 with $df (15)$. This means, regardless of the type of business that a firm is involved in, the time of entry or duration that one has been operating will determine the firms' market share. Similarly, there was a positive relationship between the type of business a firm is involved in and the cost of entry determines the profit of a firm; $p=.0005$, chi-square (X^2) of 57.613 with $df (20)$. This shows the cost of entry determines the profit of the firm regardless of the type of business involved. The strongest significant was on whether the economies of scale determines the profit of the firm regardless of the type of business oil firms were involved in in South Sudan; $P=.0005$, chi-square (X^2) of 75.341 with $df (15)$. This portray, the profit of an oil firm is highly determined by economies of scale regardless of the type of business. On whether technology required for operation can prevent a firm from operating a chi-square test shows a strong relationship; $P=.0005$, chi-square (X^2) of 74.517 with $df (20)$. This portrays technology as a key factor required for firms to operate in South Sudan oil field especially in oil waste management, oil processor and oil mining.

Ownership and Branches of oil Firms on Threat of New Entrants:

Oil firms operating in South Sudan are either owned locally, internationally, as a joint venture or government owned. A chi-square test on ownership of the firm and threat of new entrants shows there is no relationship between the two as indicated in table 4.9: economies of scale determine market share and ownership of oil firm ($p=.514$, $X^2 =8.174$, df of 9); time entry/duration of operation and ownership of the firm ($p=.312$, $X^2 =10.494$, df of 9); cost of entry determines the profit of a firm and ownership of the firm ($p=.056$, $X^2 =20.664$, df of 12); economies of scale determine profit and ownership of the firm ($p=.051$, $X^2 =21.001$, df of 12); operation technology required can prevent a firm from operation and ownership of the firm ($p=.450$, $X^2 =11.946$, df of 12). This means, the ownership of oil firm operating in South Sudan has no significant effect on the threat of new entrants.

However, there was no significant relationship ($p > .05$) between operating firms having branches in other countries and other variables under threat of entry. In summary, the findings of the relationship between: oil firm have branches outside South Sudan and economies of scale determine market share ($p = .704$, $X^2 = 1.406$, df of 1); oil firm have branches outside South Sudan and time of entry/duration of operation determines profit ($p = .142$, $X^2 = 5.447$, df of 3); oil firm have branches outside South Sudan and economies of scale determine profit of the firm ($p = .423$, $X^2 = 3.879$, df of 4); oil firm have branches outside South Sudan and operation technology required can prevent a firm from operation ($p = .560$, $X^2 = 2.990$, df of 4). This shows among all the items under threat of new entrants, only 'the cost of entry determines the profit of a firm' has positive correlation with oil firm having branches outside South Sudan.

Threat of New Entrants Influence on Performance:

In order to determine the level of influence threat of new entrances have on performance of the oil industry in South Sudan, multiple regression was conducted. With performance as independent variable and threat of entrants as dependent variable, multiple regressions show how new entrants affects and predicts performance of oil firms. The model summary, the model fits the data with positive correlation between threat of entrants and performance at $r = .596$ and coefficient of determination, R-square (r^2) = .355 with Sig F Change $p = .0005$ of 35.281. Based on the model, 35.5% of performance outcome can be explained based on threat of new entrants in the oil industry in South Sudan while the remaining 64.7% of performance are caused by other variables.

The ANOVA table shows the regression model is better in predicting the outcome variable than the mean outcome ($p = .0005 < p = .005$; $F = 35.281$, $DF = 1$, $p < .05$ at .0005). Further, the residual outcome of mean square is smaller than the regression. This shows the regression model constructed is better in predicting the outcome variable of the equation than predicting the outcome using mean equation.

The regression coefficients model 1, the analysis shows that the threat of entrants statistically predicts value of performance (Beta = .596, $t(65) = 5.940$, $p = .0005 < .005$). The beta weight gauges the importance of explanatory variable across the model and is positive on the threat of new entrants Beta of .596 and statistically significant at $p < .05$. This means, one unit of increase in threat of new entrants increases the unit of performance by .765 with or without the influence of moderating variable. The output equations are;

The general form of the regression model that was used was of the form:

$$Y = \beta_0 + \beta_1 x_i + \varepsilon$$

Hence forms the coefficient table threat of entrant significantly affect performance of oil in South Sudan with the equation

$$Y = 1.083 + .596X + .129$$

5. CONCLUSION

Generally, factors relating to threat of new entrants affect oil performance in South Sudan. These factors are: economies of scale determine profit, operation technology required can prevent a firm from operation, cost of entry determines the profit of a firm, economies of scale determine market share, and duration of operation affects firm performance. The study found out a positive relationship between type of business; oil mining, oil processor, oil distribution, oil waste management, and oil piping with: economies of scale determines the market share, cost of entry determines the profit of a firm, operation technology required can prevent a firm from operation, and economies of scale determines the profit of the firm. This lead to the conclusion that new entrant affects performance of oil industries regardless of the type of business that they are involved in. Similarly, the study concludes, oil branches determines the cost of entry, the profit of a firm and the type of business to be involved in. Also, ownership and duration of operation has no significant effect on any of the factors relating to threat of entrants. Finally, the study concludes threat of new entrance have significant influence on performance of oil industry in South Sudan.

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