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

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BY

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ABSTRACT

Increased globalization and competition has led to the rise of mergers and acquisitions for firms seeking competitive advantage in their respective industries. Competitive advantage means that, the firms can extend their margins and market share worldwide. The general objective of this study was to determine the effects of mergers and acquisitions on the financial performance of commercial banks in Kenya. The specific objectives were: to determine the effect of asset management on financial performance; to establish the effect of shareholder's equity on financial performance and to investigate the effect of financial stability on financial performance.

The study was focused on commercial banks that had merged or undergone acquisition between the period 2008 and 2016in Kenya. The study adopted a descriptive research designto determine the relationship between the variables within a population. The population of the study consisted of financial institutions in Kenya that had either merged or undergone acquisitions from 1989 to 2017 as approved by the Central Bank of Kenya.The sample was selected using the purposive method which involved studying ten commercial banks that had merged between the years 2008 to 2016. Secondary data, three years before and three years after the event was calculated from the banks' audited financial statements, bank supervision annual reports published by Central Bank of Kenya, and the respective bank websites. Data analysis method included descriptive statistic, correlation and regression analysis methods. Statistical Package for Social Sciences(SPSS) version 21 was used as the data analysis tool.

The findings oncorrelation analysis between performance and return on assets indicated a positive significant relationship ($r = 0.007, < p = 0.05$). This indicated that, return on assets as a determinant of performance of Kenyan commercial banks positively influenced mergers and acquisitions. The more the merged institutions acquired assets, the better they performed. Regression results of post-merger ANOVA indicated an R^2 of 0.287, indicating that28.7% of the variations in performance were explained by return on assets after the merger or acquisition event.Results also showeda slight rise in the mean values for return on assets after the merger.

Findings on the effect of shareholder's equity on financial performance revealed a positive correlation relationship between return on equity and performance ($r = 0.041, < p$

= 0.05). This implied that institutions that had either merged or undergone acquisition with higher shareholder's value had a higher financial performance hence higher market share. The study findings on regression analysis indicated that most of the sampled banks had an increase in return on equity after the merger or acquisition with a variation of only 0.4% explaining performance.

Results on the effect of financial stability on financial performance indicated a significant negative correlation (r = 0.405,> p =0.05). Meaning that, the higher the capital adequacy ratio an institution has, the lower the financial performance of the institution. The results also indicated that some of the sampled banks posted an increase in the capital adequacy ratio while others posted a decrease after the merger event. Regression results indicated that only 3.2 % of the variations in performance were explained by capital adequacy ratio after the merger or acquisition.

The study concluded that there was a significant relationship between financial performance and return on assets, there was no significant relationship between financial performance and return on equity and there was also no significant relationship between financial performance and financial stability of institutions that had either merged or undergone through acquisition.

The study recommended that the banking institutions work on raising their return on assets, return on equity and capital adequacy ratios. To raisereturn on equity it was recommended that management should work on reducing the company's operational costs and sell off fixed assets that are not being used. To increase return on equity, the study recommended increasing the overall profit generated and the amount of debt capital and reduce the excess cash on the balance sheet by paying out dividends to its shareholders. The study proposed that capital adequacy ratio be increased by issuing new equity through rights issue to existing shareholders and by replacing riskier or more expensive loans with safer ones such asgovernment securities. The study also recommended that further studies be carried out on the effect of mergers and acquisition on financial performance from time to time to establish trends for longer periods and to capture new opportunities that have recently emerged in Kenya.

ACKNOWLEDGEMENTS

DEDICATION

This research project is dedicated to my family for their unconditional love and support.

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LIST OF ABBREVIATIONS

CAR	Capital Adequacy Ratio
CBK	Central Bank of Kenya
GE	General Electric Company
HSBC	Hong Kong and Shanghai Banking Corporation
IBM	International Business Machines
J&J	Johnson & Johnson
KPMG	Lynell Peat Marwick Goerdeler
MSI	Market Share Index
M&A	Merger and Acquisition
NSE	Nairobi Stock Exchange
NXP	Next Experience
P&G	Proctar and Gamble
ROA	Return on Assets
ROE	Return on Equity
SBM	State Bank of Mauritius
SPSS	Statistical Package for Social Sciences

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1.0   INTRODUCTION

1.1.   Background of the Study

Mergers and Acquisitions (M&A) have become popular in Kenya for firms who wish to gain a competitive advantage in their various industries such as banking, insurance, oil, gas, electricity among others (Kemal, 2011). Mergers and Acquisitions are increasing worldwide because they encourage competition among industry firms, they also reduce business risk and increase market share of the firms. Mergers and Acquisitions are types of strategic decisions made by top most management which affect the long-term performance of the business. Such decisions carry higher levels of risk and if effectively implemented, they can reward highly (Buono, 2003). M&A are alsocorporate strategies used by firms to promote future growth and create sustainable value (Wang & Xie, 2008).

From a legal perspective, mergers can be defined as a combination of two or more firms, often comparable in size, in which all but one ceases to exist legally. An acquisition on the other hand occurs when a company takes a controlling interest in another company, a legal subsidiary of another firm, or selected assets of another firm (DePamphillis, 2014).

A direct or statutory merger is one which the acquiring company assumes the assets and the liabilities of the company being acquired according government policies in that country. A subsidiary merger involves the target company becoming a subsidiary of the parent company. A statutory consolidation consists of two or more companies joining to form a new company (Cassim, 2008). There are three major types of mergers and acquisitions; horizontal, vertical and conglomerate mergers. Horizontal merger occurs when two or more competing firms producing and selling the same product merge. Since their products are considered as the same by their buyers, their cross elasticity of demand and supply is usually high. The second type of merger is the vertical merger. It occurs between firms that operate at different stages of production and have a successive functional link for final product. The third type of merger is the conglomerate merger, whichoccurs between firms that run unrelated business activities (Galpin & Herndon, 2014).

The global performance of M&A market has been adversely affected by ongoing political and regulatory changes worldwide. Despite this, acquirers across the globe have leveraged strategic combinations to expand their geographic reach and innovation

capabilities, such as Qualcomm's acquisition of NXP (Next Experience) Semiconductors, Chem China's acquisition of Syngenta, London Stock Exchange's merger with Deutsche Boerse Group and American Telephone & Telegraph (AT&T) acquisition of Time Warner (Morgan, 2016). Other global companies like Proctar and Gamble (P&G), Johnson & Johnson (J&J), International Business Machines(IBM), General Electric Company (GE), Pfizer, Cisco, Tata & Sons, Mahindra & Mahindra, Haier, Lenovo, and Hong Kong and Shanghai Banking Corporation (HSBC) among others, have all adopted a M&A strategy. According to researchers, such organizations rely on three mechanisms to achieve growth: organic growth, alliances, and mergers and acquisitions (Rosinski, 2011). Cross-border M&A continue to be an important feature of the market, accounting for 36% of total volume versus 31% in 2015. A surge in China's foreign business contributed to overall cross-border M&A growth, as Chinese companies sought attractive opportunities abroad (Morgan, 2016).

The African M&A market has been trending upwards over the past few years, although it is quite small compared to other M&A markets worldwide. This has been mainly due to the high economic growth in energy, mining and utilities sectors. It has been noted that most cross-border mergers take place among firms in developed countries and that firms with high levels of intangible assets or research and development (R&D) intensity are natural candidates for cross-border mergers (Sonenshine &Reynolds, 2014). This is due to the following; the combined firm needs to spread the high fixed cost of R&D expenditures and knowledge asset attainment over large foreign markets. Global Law firm Baker McKenzie's latest quarterly Cross-border M&A Index shows that South Africa was the top target country for inbound deals by volume and value, accounting for 29% of total deal count and USD 422 million or 54% of total value in Africa. The report also showed that Nigeria had an upward trending on M&A trend followed by Kenya. Examples of major African M&A deals in Africa include: Algeria's Orascome Telecom Algerie (OTA) acquisition by Egypt's Global Telecom Holding and South Africa's Neotel acquisition by Vodacom; a subsidiary of telecommunications giant Vodafone.

At the time of the study, there were a total of 42 commercial banks, 12 microfinance banks and 1 mortgage finance institution in Kenya. All these banks are regulated by the Central Bank of Kenya, with additional oversight from the Capital Markets Authority (CMA). All the listed banks are required to adhere to certain regulations such as

minimum liquidity ratios and cash reserve ratios with the Central Bank (Cytonn Investments Report, 2015). Central Bank of Kenya (CBK) is tasked with formulating and implementation of monetary and fiscal policies and is the lender of last resort in Kenya and is the banker to all other banks. It ensures proper functioning of the Kenyan financial system, the liquidity in the county and the solvency of the Kenya shilling. To address issues that affect the Banking industry in Kenya, local banks came together and formed a forum under the Kenya Bankers Association in 1962.

Commercial banks in Kenya have the following functions (Ongeri, 2013): they keep the money deposited and valuable items in safe custody and make it accessible to customers when they need it, they facilitate the transfer of funds from one account to another within the same bank or to a different bank, they offer lending services to customers who need the money at an interest, they offer foreign exchange services and assist, they offer advisory services on financial matters relating to loans and taxation matters. The banks also offer their customers investment services such as selling shares on behalf of investors. They can also sell their own shares to the customers thus offering them investment opportunities. Lastly, commercial banks act as trustees.

The major issues facing the Kenyan banks include: Implementation of new regulations that were passed after adopting the new constitution. According to the Kenya National Bureau of Statistics (KNBS) 2016 report, the amendment of the Banking Act in August 2016 to cap the lending rates to a maximum of 4% above the Central Bank Rate (CBR) resulted in a substantial decline in the interest rates during September 2015 from a percentage of 16.75% to 13.84% in the same month. The Global crisis has also affected the banking industry in Kenya and more so the mobilization of deposits and trade reduction. The Interest margins declines have also affected the banking industry in Kenya.

The Banking industry in Kenya is governed by the Banking Act, the Companies Act, the Central Bank of Kenya Act and the various guidelines issued by the Central Bank of Kenya (Central Bank of Kenya 2014 annual report). Mergers and acquisition trends in Kenya suggest a growth in the financial services sector in recent years, whereas sectors such as manufacturing, tourism and healthcare have not seen a significant deal activity (KPMG Annual Report, 2016). Kenyan Banks have realized a tremendous growth on

financial performance in the last five years and have expanded to the east African region. This has led to automation as a way of moving from the traditional banking to meet the growing complex needs of their customer and globalization challenges. Another factor that has led to financial performance growth in the banking industry in Kenya includes: Banks responding to the needs of the Kenyan market for convenience and efficiency through alternative banking channels such as mobile, internet and agency banking. Industry-wide branch networking expansion strategies in the East African community region is another factor that has also led to growth (Cytonn Investment Report, 2015).

The banking industry in Kenya has experienced an unprecedented level of consolidation especially since the 1990s due to economic growth. Between the years 2000 to 2015, a total of 20 companies have engaged in either a mergers or acquisitions (Gathuku &Njeru, 2015). Some of the financial institutions that have merged with other firms include; Kenya Commercial Bank Ltd, CFC Stanbic, Paramount Universal Bank, Citibank NA, Southern Credit Banking Corp. Ltd., Co-operative Bank of Kenya ltd, Investment & Mortgage Bank Ltd., Prime Bank Ltd., Commercial Bank of Africa ltd, EABS Bank ltd., Kenya Commercial Bank Limited, Jamii Bora Bank Ltd., Equatorial Commercial Bank Ltd. and Dubai Bank Ltd. Other companies that have acquired others include; Bank of Africa Bank Ltd., Eco bank, Guaranty Trust Bank (Kenya) Ltd, K-Rep Bank Ltd and Equatorial. Recent merger/acquisition deals that have taken place as indicated on 2017 annual report for Central Bank of Kenya include Fidelity Commercial Bank acquisition by SBM (State Bank of Mauritius) Kenya Ltd, Habib Bank Kenya acquisition by SBM Bank Kenya Ltd and Habib Bank Kenya Ltd acquisition by Diamond Trust Bank Kenya Ltd.

1.2. Statement of the Problem

Before the standardization of interest rates, Kenyan banks were making huge profits as seen on their financial statements (Kenya & Konya, 2015). Despite the upward trend, they still faced a few challenges such as; ATM card skimming where banks are making losses compensating customers who are being ripped off their money by fraudsters, there has also been a lot of theft cases in the banking industry from their own employees, their security providers, and other external individuals (Cabric, 2015). Local mobile money transfer services such as Mpesa, Airtel and currently introduced Equitel money have brought in a lot of competition to banks. Many of their customers are making savings on

their phones as opposed to traditional banking (Cytonn Investment report, 2015). Mugambi (2014) did a research on a similar study; 'The impact of mergers and acquisitions on the financial performance of commercial banks in Kenya'. The population of his study consisted of fourteen banks that had merged in the period 1998 to 2013 in Kenya. Results indicated that there was improvement in financial performance of commercial banks after a merger or acquisition. This was due to an increase in return on assets, return on equity and reduction in cost to income ratio after the merger. Different studies on mergers show conflicting results on the financial implication of mergers and acquisitions in the banking industry in Kenya.

With increasing competition and the economy heading towards globalization, the trend on mergers and acquisitions are expected to rise at a much larger scale with the aim of achieving a competitive edge in the industry (Mender, 2014). There are few considerations that a company should consider before getting into a merger or acquisition; the company should be willing to take the risk and make investments to benefit fully from the merger as the competitors and the industry take heed quickly (Bryman & Bell, 2015). To reduce and diversify risk, multiple decisions must be made to narrow down to the one that will succeed. Management of the acquiring firm must also learn to be patient and be able to adapt to the change (Cameron & Green, 2015). Previous studies have mainly looked at return on equity and return on assets as measurable independent variables to measure performance while leaving out financial stability as a measure. This study, therefore investigated the effects of mergers and acquisitions on financial performance of commercial banks in Kenya between the years 2008 to 2014 where financial performance was measured using three variables; shareholders' value, asset management and financial stability. An analysis of three years before and three years after their mergers or acquisition was done.

1.3. General Objective of the Study

The general objective of this study was to establish the effect of mergers and acquisitions on the financial performance of commercial banks in Kenya.

1.4. Specific Objectives of the Study

The following specific objectives were used to guide the study:

1.4.1. To determine the effect of shareholder's equity on financial performance of acquisitions or merged commercial banks in Kenya.

1.4.2. To determine the effect of asset management on financial performance of acquisition or merged commercial banks in Kenya.

1.4.3. To investigate the effect of financial stability on financial performance of acquisition or merged commercial banks in Kenya.

1.5. Importance of the Study

1.5.1. Commercial Banks

This study is important for commercial banks that have merged and wish to improve on their financial performance.

1.5.2. Investors and Institutions

This study is important to investors and institutions who wish to make decisions concerning mergers or acquisitions.

1.5.3. Policy Makers

This study will help policy makers to maximize on the value of the concerned stakeholders based on the merger and acquisition strategy implemented by the organization.

1.5.4. Scholars and Researchers

The study will also benefit scholars and researchers who wish to understand the relationship between mergers/acquisitions and the performance of commercial banks.

1.6. Scope of the Study

The population of the study consisted of financial institutions in Kenya that had either merged or undergone acquisitions from the period 2008 to 2016 as approved by the Central Bank of Kenya. The study focused on ten commercial banks located in Nairobi.

The study was limited to the financial sector only because it focused on mergers and acquisitions of banks and financial institutions that took place between theperiods 2008 to 2016.

1.7. Definition of Terms

1.7.1. Mergers and Acquisitions (M&A)

Merger is the activity by which two or more companies decide to come together and function as one to achieve strategic objectives or goals like resource sharing, resource utilization, economies of scale or cost minimization or any other operational or financial advantage for both the companies (Salim, 2011).The term "acquisition" is used to refer to any takeover by one company of the share capital of another in exchange of cash, ordinary shares, or loan stock (Halpern, 1983).

1.7.2. Commercial Banks

A commercial bank is a financial institution that provides various financial services, such as accepting deposits and issuing loans (Mbwaya, 2012).

1.7.3. Shareholders Value

This is the value delivered to shareholders because of management's ability to grow sales, earnings and free cash flow over time (Fernandez, 2015)

1.7.4. Efficiency

This relates to how well an organization transforms inputs into outputs. To measure efficiency, it is necessary to compare actual organizational production to some standard or benchmark that, if achieved, is considered efficient (Reda, 2013).

1.7.5. Performance

This is the process of quantifying the efficiency and effectiveness of an action. Organizational performance can be achieved by comparing the value that an organization creates using its productive assets with the value that owners of these assets expect to obtain (Armstrong &Baron, 2005).

1.7.6. Financial Performance

The level of performance of a business over a specified period of time, expressed in terms of overall profits and losses during that time. Evaluating the financial performance of a business allows decision-makers to judge the results of business strategies and activities in objective monetary terms (Ang, 2014)

1.8. Chapters Summary

This chapter introduced thestudy on the effect of mergers and acquisitions on financial performance of commercial banks in Kenya. The background discusses global trends and what is happening in Africa regarding M&A. A summary of the banking industry in Kenya has also been discussed to show the M&A trends locally. Thestatement of the problem has been explored with an aim of developing the general objective of the study. Specific research objectives, the significance and scope of the study were also included. Chapter two discusses literature review from different authors related to mergers and acquisitions. Chapter three discusses the methodology used, while chapter four discusses the results and findings of the study. Finally, chapter five discusses the results, conclusions and recommendations of the study.

CHAPTER TWO

2.0. LITERATURE REVIEW

2.1. Introduction

This chapter presents a review of literature on the effects of mergers and acquisitions in the performance of financial institutions. It presents literature on the effects of shareholder's equity on financial performance, effect of asset management on financial performance and effects of financial stability on financial performance.

2.2. Effects of Asset Management on Financial Performance

2.2.1. Asset Management and financial performance

Asset management is defined as the way in which the acquisition, use and disposal of the assets of an individual or a company are managed in order to maximize profits (Ang, 2014). It is also concerned with the efficient utilization of the organization's investment in both physical and human asset to guarantee profit maximization objective of the firm (Moynihan & Pandey, 2010). Empirical studies suggest that asset management in commercial banks is determined by the ability of the banks to balance the capital structure by retaining capital, absorbing loan losses, supporting future growth of assets and providing return to investors (Makau & Memba, 2014). Giandomenico(2012) did a study on asset liability management in banks for the period2004 - 2011 using a panel of over 30 banks across Europe. The study concluded that to be effective in banking, the management of assets and liabilities must take into consideration the earnings, liquidity, profit and the level of loans & deposits.

Suzuki (2011) focused on financial reforms, ownership and performance in the banking industry: the case of Indian Commercial Banks. The study was undertaken to investigate the performance of commercial banks after the implementation of significant financial reforms. The results generated by regression models indicated that foreign ownership hadappositivesignificant impact on bank performance. He found that private ownership has favorable impact on income efficiency, return on assets and non-performing loans. The same had a negative impact on cost efficiency. Nazir and Afza (2009)studied the impact of different types of working capital management policies on financial performance of firms in different sectors in Pakistan. Their study used a sample of 263 non-financial firms belonging to 17 different sectors listed at the Pakistan stock exchange from1998 to 2003. Secondary data was collected from the financial reports of the selected

companies and from the publications of State Bank of Pakistan. For the measurement of the degree of aggressiveness they used current liabilities to total assets ratio and current assets to total assets ratios. To investigate the impact of policies on the performance of firms, they used return on equity and return on assets. Using regression analysis, results confirmed an inverse relationship between degree of aggressiveness of the policies and profitability.

Afza and Nazir (2008) conducted another study on working capital approaches and firm's returns. Their results showed a negative relationship between the profitability measures of the firm and the degree of aggressiveness of working capital management. Their study consisted of Pakistani firms listed under sixteen industrial groups in the Karachi Stock Exchange (KSE) for the period (1998-2005). Findings indicated that firms with more aggressive working capital policieswere not be able to generate more profit, proving the negative relationship of working capital management and profitability.

2.2.2. Modigliani & Miller (M&M) theorem

The irrelevance theory of capital structure (1958) introduced by Merton Miller and Franco Modigliani (M&M) was the first breakthrough in relation to the subject of capital structure and its effect on firm performance. They first hypothesized that if markets are perfectly competitive, firm performance will not be related to capital structure, therefore suggesting no significant relationship between a firm's capital structure and its performance. The value of the firm is similarly unaffected by its financial structure. Their assumptions of a perfectly competitive market excluded the impact of tax, inflation and transaction costs associated with raising money. In addition, they also assumed that disclosure of all information is credible, thus there is no information asymmetry (Hamada, 1969; Rothschild &Stiglitz, 1974). There were various criticisms, which encouraged M&M to issue an alteration to their first theory, which was referred to as MM2. In their revised proposition, they incorporated tax benefit as a determinant of capital structure.

The vital characteristic of taxation is the acknowledgement of interest as a tax-deductible expenditure. According to M&M a company that respects its tax obligations, benefits from partially offsetting interest, namely the tax shield, in the form of paying lower taxes. The M&M theory indicated that companies could maximize their value by employing

more debt due to the tax shield benefits. Hence, firms benefit from taking on more leverage. M&M show that firm value and firm performance is an increasing function of leverage due to the tax deductibility of interest payments at the corporate level (Modigliani & Miller, 1963). In reality markets are inefficient due to taxes, information asymmetry, transaction costs, bankruptcy costs, agency conflicts and any other imperfect elements. When taking these elements into consideration, the M&M theorem tends to lose most of its explaining power. Even though the theory was heavily criticized of some weaknesses and its irrelevant assumptions of the real world, this theory still provides the foundation for many other theories suggested by other researches.

2.2.3. Static trade-off theory

According to Kraus and Litzenberger (1973), the Static Trade-off theory assumes that a firm will tradeoff the benefits, costs of debt and equity financing to find an optimal capital structure after accounting for the market imperfections. Such include taxes, bankruptcy costs and agency costs. The theory also states that there is a benefit to financing with debt, specifically the tax benefit. However, there is also a cost of financing with the debt, namely the indirect bankruptcy cost. There is a maximum point where the marginal benefit of further increase in debt declines as debt increases, whereas the marginal cost increases. Hence, this static trade-off theory of capital structure states that optimal capital structure is obtained where the net tax advantage of debt financing balances leverages related costs such as financial distress and bankruptcy, holding a firm's assets and investment decisions constant.

Baxter (1967) and Altman (1968) in view of this theory claim that issuing equity means moving away from the optimum and therefore should be considered bad news. According to Myers (1984), firms adopting this theory could be regarded as setting a target of debt-to-value ratio with gradual attempt to achieve it. However, managers will be reluctant to issue equity if they feel it is undervalued in the market. The consequence of this is that; investors will perceive equity issues to only occur when equity is either priced or overpriced. Leverage is able to enhance a firm's performance by limiting conflicts between shareholders and managers because of having excess cash. El-Sayed Ebaid (2009) argued that leverage mitigates lower agency costs, since the firm's reputation and the managers' wages are at stake. On the other hand, higher leverage could also mean that the firm has higher commitment to fulfill its future obligations, in terms of principal

and interest payments. Furthermore, higher leverage ratios also lead to higher costs relating to financial distress.

Miller (1977) documented that the cost related to financial distress is not material compared to the benefits of higher leverage ratios. Moreover, the trade-off theory suggests that those firms with higher levels of retained earnings, i.e. profitable firms, tend to have higher debt levels because they can more effectively use the tax shields on interest. Since these companies have higher operating profits, the probability and costs of financial distress for them is lower. Consequently, the trade-off theory expects a positive association between firms' leverage ratios and their financial performance (Chakraborty, 2010). Wippern (1996) investigated the relationship between financial leverage and a firm's performance. In his study he used debt to equity ratio as financial leverage indicator and earnings to market value of common stock as performance indicator. His results indicated that leverage had a positive effect on firm performance. Capon et al. (1990) conducted a meta-analysis from 320 published studies related to financial performance; they found a positive relationship between usage of leverage levels and financial performance.

Roden and Lewellen (1995) analyzed the impact of capital structure on performance for 48 US based firms with a leveraged buyout during the period 1981 - 1990, using multinomial logit models. Their results indicated a positive relationship between firm performance and its leverage policy based on tax considerations. Their findings therefore are consistent with the trade-off theory. Moreover, there is a positive relationship between financial leverage and expected performance (Dessi & Robertson, 2003). They argued that low growth firms attempt to depend on borrowing to exploit the expected growth opportunities by investing the borrowed money in profitable projects which results to an increase in the firm's performance. Aburime (2005) carried out regression analyses to analyze the impact of leverage ratio on firm performance between Ghanaian listed firms over the period 1998 to 2002. Throughout his analysis, he compared the capital structures of publicly quoted firms, large unquoted firms and small and medium enterprises. He based his models on three measures of leverage, namely, short-term debt over total assets, long-term debt over total assets and total debt over total assets. His results indicated that there existed a significantly positive relationship between the short-term and total debt and return on equity.

All the previously mentioned mechanisms suggested that the pecking order theory claims a negative relationship between capital structure and firm performance, since more profitable firms opt to use internal financing over debt (El-Sayed Ebaid, 2009).

2.3. Effects of Shareholder's Equity on Financial Performance

This section looks at what is shareholder equity and relevant theories on shareholders' equity. Shareholder wealth maximization has also been included in this section. Empirical studies suggest that mergers tend to increase shareholders' equity but decrease efficiency for the target firm (Li, 2016). Oladipupo and Okafor (2011) explain that increasing shareholders' wealth is the fundamental purpose of mergers and acquisitions, although different banks have different motives for participating in mergers. For example, due to unforeseen political and economic circumstances in Kenya in 2007, it was a strategic move for banks to merge so that smaller banks could operate within the foreseeable future and avoid bank runs (Sharma, 2011). Synergy is another motive and the most common reason for mergers whereby, the value of two firms combined is greater than one. Synergy amalgamates duplicate costs by replacing identical processes acquired from the target firm and can be considered that the merged organization could exceed the profits of the original company by reducing costs or increasing the average income (Shaver, 2006).

Tax benefits are another motive where companies can reduce taxes when merged. Tax benefits can accrue at both the corporate and at shareholder levels (Dennis, 2016). For example, acquiring firms can claim back their earnings when used to offset against the taxable profits. A target firm and shareholders can benefit by receiving profits when selling their shares during the process of the merger (Ghosh, 2004). Costs saving motives also drive the merger activity, for example having a diversified production strategy will reduce operational costs. This diversification will lead to new sources of cash flow because the merger will increase and enhance the range of bank products and services available to customers as new markets are entered (Badik, 2007).

2.3.1. Shareholders' Equity and financial performance

Shareholders' equity also known as net worth or stockholders' equity represents the net value of an organization. It is the amount that would be returned to shareholders if all the company's assets were to be liquidated and all its debts repaid. Shareholders' equity can

be either negative or positive (Moctar & Xiaofang, 2014). A positive figure means that the company has more than enough assets to cover its liabilities while a negative figure means that the company's debts outweigh its assets. On the other hand, shareholders' wealth is the present value of the expected future returns to the shareholders of the firm (Brigham 2014).

Rani, Yadav, and Jain (2011) conducted a study on the impact of Mergers and Acquisitions on Shareholders' Wealth in the Short Run: An Event Study Approach and came with the following findings; the earlier the investor sells, the more he gains, and issuance of stock isn't always the best decision for an investor. Hypothetically, an investor can earn substantial returns if the shares of the acquiring company are purchased two days before the announcement day and oversubscribed two days after the announcement day. The announcement of cross-border acquisitions provides abundant higher returns than that for domestic acquisitions. Additionally, the accumulative abnormal returns within the case of cross-border acquisitions are known to be permanent, whereas within the case of domestic acquisitions they're temporary. The announcement of complete acquisitions of the target firm as a wholly-owned subsidiary provides higher returns than that for partial/majority management acquisitions. Finally, the announcement of acquisitions financed with cash payment provides substantial returns. Weston and Weaver (2001) suggested that the shareholders of the acquiring firms gain from efficiency enhancing mergers. Moeller, Schlingemann, and Stultz (2004) report that small acquirers experience significantly higher capital/asset ratio around M&A announcements than large acquirers.

Financial and economic studies typically employ event studies, which aim at understanding how the share prices (stock returns) of the firms concerned react to the merger or acquisition announcement. The results of these studies suggest that mergers and acquisitions lead to significant positive abnormal returns to shareholders of the target firm while resulting in negative abnormal returns to shareholders of the bidder firms (Bild & Guest, 2002). The studies also demonstrate that despite the negative abnormal returns to acquiring shareholders, these shareholders eventually benefit from overall significant gains in the future. These results have led some authors to argue that the results obtained tend to be sensitive to the methodology employed thereby leaving one to

continue doubting whether the results reflect reality or whether they simply reflect the authors' beliefs about mergers and acquisitions (Brigham 2014).

2.3.2. Shareholders Wealth Maximization Theory

Shareholder Wealth Maximization model (SWM), proposes that the single goal of the firm should be to maximize the return to shareholders for a given level of risk, or conversely, minimize the risk to shareholders for a given rate of return (Jensen &Ruback, 1983). With this in place, the firm will be able to increase its financial performance. This theory assumes that the shareholders can eliminate all random type risks, except the risk of overall stock market movements, through portfolio diversification. International portfolio diversification is the ultimate method of this type of risk reduction (Ansong, 2015). The SWM model assumes the traditional belief that the stock market is efficient (Jensen, 1978). This market efficiency assumes that the equity share price is always correct because it captures all the new information on return and risk as perceived by investors, and quickly incorporates this new information into the share price. Share prices are in turn, the best allocators of capital in the macro economy (Shah & Arora 2014). Shareholder's contract with management is to maximize shareholders wealth (Bambale, 2016).

Shareholder wealth maximization is a norm of corporate governance that encourages a firm's board of directors to implement all major decisions such as compensation policy, new investments, dividend policy, strategic direction, and corporate strategy with only the interests of shareholders in mind (Migitha, 2016). There is a strong support for the idea that shareholder wealth maximization should be the primary norm underlying the governance of profitable corporations with objective of increasing their financial performance (Diz, 2014). Managers who strive to maximize their own interests rather than the firm's profits are likely to be replaced by the shareholders of the firm.

2.3.3. Advantages and Disadvantages of Shareholders' Wealth Maximization

Firstly, wealth maximization is based on cash flows and not profits. Unlike the profits, cash flows are exact and definite and therefore avoid any ambiguity associated with the accounting profits. Secondly, profit maximization is short-term while wealth maximization is a long term goal. Thirdly, wealth maximization considers time value of money (Migitha, 2016) while profit maximization does not. A dollar today and a dollar

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one-year later do not have the same value. In wealth maximization, the future cash flows are discounted at an appropriate discounted rate to represent their present value. Fourthly, the wealth-maximization criterion considers the risk and uncertainty factor while considering the discounting rate. The discounting rate reflects both time and risk. The higher the uncertainty an organization experiences, the higher the discounting rate and vice-versa. Pursuing a profit maximization strategy comes with the obvious risk that the company may be so entrenched in the singular strategy meant to maximize its profits that it loses everything if the market takes a sudden turn (Shah & Arora, 2014).

A company focused on maximizing its profit may miss out on opportunities for investment and expansion. If a company pursues a profit maximization strategy, it creates an environment where the price is given a priorityand therefore cutting costs becomes the primary goal of the organization. This in turn,could lead to a loss of goodwill with customers and suppliers. It also creates an expectation for shareholders to see immediate gains, rather than realizing profits over time (Migitha, 2016). When maximizing profit is the primary goal, investments, reinvestments and expansions are typically put aside. The company simply utilizes what it has. This can create a more cost-efficient environment. In the meantime, the profits keep building, producing a healthy bottom line and increase the firm's financial performance. Sometimes profit maximization is used entirely to create an influx of cash so the firm can reduce its debt or save up for expansion. Some degree of profit maximization is always present. Moreover, investors and financiers in the company may require a certain level of profits to secure funds for expansion. Furthermore, a company must perform well for its shareholders because they expect a return on their investments.

2.4. Effect of Financial Stability on Financial Performance

A financially stable organization is one that is capable of efficiently allocating its resources, being able to assess and manage its financial risks. Systematic loss is one way which can be used to measure financial stability. It combines three key elements: each individual institution's probability of default, the size of loss given default, and the nature of defaults across the institutions due to their interconnections (Sherraden & Ansong, 2016). Other indicators of financial stability include the ratio of regulatory capital to risk-weighted assets and the ratio of non-performing loans to total gross loans. Risk-weighted assets (RWA) has become one of the banking's most important yardsticks. Lowering a

bank's RWAs means less equity is required, which translates to higher returns and better financial performance.

2.4.1. Capital Requirements and Financial Stability

Rationale for capital requirements regulation is motivated by the concern that a bank may hold less capital than is socially optimal relative to its riskiness. In theory, the stabilizing effects of capital requirements are supported by models based on the option-pricing model (Galai & Masulis, 1976). In this framework, an unregulated bank will take excessive portfolio and leverage risk to maximize its shareholder value at the expense of the deposit insurance (Keeley & Furlong, 1990). Capital requirements can reduce these moral hazard incentives by forcing bank shareholders to absorb a larger part of the losses, thereby reducing the value of the deposit insurance put option. With more capital and less risk-taking, the effect is clearly a decrease in the bank's default probability.

The ability of capital requirements to strengthen the stability of the banking system has been challenged in models based on the mean-variance framework. Sherraden and Ansong (2016) found that if capital is relatively expensive, the forced reduction in leverage diminishes the bank's expected returns and hence reduces performance. Consequently, the bank's owners may choose a higher point on the efficiency frontier, with a higher return and a higher risk. In some cases, the increase in the bank's risk over compensates the increase in capital and leads to a higher default probability. The introduction of risk-based capital standards can be considered as an attempt to eliminate the possible perverse effects of capital requirements. Unfortunately, empirical evidence indicates that current capital requirements do not reflect banks' risk-taking accurately.

Avery and Berger (1991), for example, find that the Basle risk-weighting framework explains only about 5% of banks' loan performance. If there are flaws in the risk-weightings, risk-based capital standards may have destabilizing effects. Banks constrained by the capital requirements can improve their capital ratio by decreasing risk in terms of the official standards while business risk is increased. In the absence of adjustment costs in the capital ratio, banks would never hold more capital than required by the regulators or by the market. In practice, however, adjusting the capital ratio may be costly. Equity issues may, in the case of information asymmetries, convey negative information to the market on the bank's economic value. Moreover, shareholders may be

reluctant to contribute new capital if the bank is undercapitalized. This would mean that most of the benefits would accrue to creditors. In the presence of these adjustments costs, banks falling under the legal capital requirements are not be able to react instantaneously (Thompson, 1990). They may then be subject to repeated regulatory penalties or even get closed. Consequently,banks may prefer to hold a "buffer" of excess capital to reduce the probability of falling under the legal capital requirements, especially if their capital ratio is very volatile. There are other papers that try to assess the costs and benefits of higher capital requirements. One example is Miles et al. (2013) who derive the optimal capital ratio for UK banks. They calculate costs using a two-step approach (first, estimate the impact of higher capital on lending spreads; next, estimate the impact of higher lending spreads on output). The key results indicated that a 1 percentage point increase in capital requirements caused theoutput to fall by 0.02%, compared with 0.09% in a study done by Angelini, Neri and Panetta (2014). In the long term, the increase in lending spreads by 1 point in the capital requirement and is equal to 0.8 basis point, which is smaller by a factor of 16 compared the estimate done by King and Baker (2010) of 13 basis points.

Given these costs and considering that higher capital also reduces the probability of a banking crisis, the welfare analysis suggested that the optimal bank capital should be around 20% of the risk-weighted assets. Benes and Kumhof (2011) use a theoretical model to analyze the impact of prudential rules and a countercyclical capital buffer requirement. When risk weights are low, they give an impression that banks are sufficiently capitalized and in sound financial health. Overoptimistic assessment of risk weights has led to large-scale extension of credit and hence a decline in lending standards. The reduction of risk weights could be particularly strong in a period in which interest rates are low. A reduction in the policy rate boosts asset and collateral values, which in turn can modify bank estimates of probabilities of default, loss given default and volatilities.

2.4.2. Buffer Theory of Capital Adequacy

Consequently, banks may prefer to hold a 'buffer' of excess capital to reduce the probability of falling under the legal capital requirements, especially if their capital adequacy ratio is very volatile. For example, capital requirements constitute the main banking supervisory instrument in Nigeria. The Central Bank of Nigeria intervenes little in banks' activities but does direct on-site examinations and at times delegates this task to

external auditors. By contrast, a breach of the capital requirements is considered a major infringement of banking legislation and is not tolerated by the Central Bank of Nigeria (Soludo, 2004). Banks remaining undercapitalized for prolonged periods are usually closed. The withdrawal of some banking license at the expiration of the recent capitalization of banks in Nigeria in 2005 is a pointer to this fact. Banks will require more capital if deposits are not fully mobilized from the public. Capital is more reliable, dependable and can be used for long term planning. Ability of banks to mobilize enough deposits obviates the capital base from being eroded (Adegbaju & Olokoyo, 2008).

The buffer theory of Calem and Rob (1996) predicts that a bank approaching the regulatory minimum capital ratio may have an incentive to boost capital and reduce risk to avoid the regulatory costs triggered by a breach of the capital requirements. However, poorly capitalized banks may also be tempted to take more risk in the hope that higher expected returns will help them to increase their capital. This is one of the ways risks relating to lower capital adequacy affects banking operations. In the event of bankruptcy of a bank, the risks are absorbed by the bank, customers and Insurance Corporation (NDIC). A study by Ikpefan (2013) on the impact of bank capital adequacy ratios, management and performance in the Nigerian commercial bank between the period1986 - 2006. The study showed that shareholders fund /total Assets ratio which measures capital adequacy of banks (risk of default) had a negative impact on return on assets. The efficiency of management measured by operating expenses indices is negatively related to return on capital.

Berger and Udell (2006) investigated whether the 8% capital backing for loans to private enterprises required by the 1988 Basle Accord, encouraged banks to reallocate their assets from such loans to government securities. Apart from Berger and Udell, other authors found evidence that the risk-based capital requirement set by the Basle Accord significantly contributed to the credit crunch. No matter the definition adopted, a bank's capital is widely used to analyze the status of its financial strength (Bobakova, 2003). Positive correlation between returns and capital has been demonstrated by Naceur (2003) and Eisenbeis and Kwan (2005) among other researchers. While investigating the determinants of Tunisia banks' performances during the period 1980 to 1995, Naceur and Goaied (2001) indicated that the best performing banks are those who have struggled to improve labor and capital productivity and those who have been able to reinforce equity.

Bourke (1989) and Naceur (2003) agree that well capitalized banks face lower need to external funding and lower bankruptcy and funding costs. These advantages translate into profitability and hence increased financial performance. This means that the more capital a bank has, the more resistant it will be to failure (Uche, 1998). Capital requirements can reduce these moral hazard incentives by forcing bank shareholders to absorb a larger part of the losses, thereby reducing the value of the deposit insurance put option. With more capital and less risk taking, the effect is clearly a decrease in the bank's default probability.

2.5.   Chapter Summary

In this chapter, theories on how financial performance is affected by asset management, shareholders' equity and financial stability have been discussed. A review of relevant literature has been used to show different views and results in respect to the objectives of the study from related studies from different researchers. The next chapter three discusses the methodology used in this study, the data collection technique and the methods that were applied in analyzing the data.

CHAPTER THREE

3.0. RESEARCH METHODOLOGY

3.1. Introduction

This chapter presents the research methodology. The research method consists of how the researcher collects, analyzes, and interprets the data in the study (Creswell, 2009). This chapter discusses the research design, population, sampling design, data collection methods, research procedure, data analysis methods and the chapter summary.

3.2. Research Design

A Research design is a master plan that specifies the methods and procedures for collecting and analyzing the needed information i.e. it provides a framework or plan of action for the research (Zikmund et al., 2013). The study adopted a descriptive research design which was focused on determining the relationship between financial performance and mergers or acquisitions of commercial banks in Kenya. Descriptive studies report on summary data such as measures of central tendency including the mean, median, mode, deviance from the mean, variation, percentage, and correlation between variables (Knupfer& McLellan, 2001). An event study methodology was used to determine the effect of mergers and acquisitions on the performance of merged financial institutions. There was the period before the study known as the pre-merger period and the period after the merger known as the post-merger period. Correlation and regression methods were then used to analyze the secondary data collected from audited financial statements, bank supervision annual reports published by Central Bank of Kenya, and the bank websites that had either merged or undergone acquisitions.

3.3. Population and Sampling Design

3.3.1. Population

Population is a group of individuals, objects or items from which samples are taken for measurement and have at least one thing in common (Kombo &Tromp, 2011). Mugenda O. and Mugenda A. (2013), state that a population is a group of individuals or objects with a common observable characteristic. The population of this study was comprised of all licensed commercial banks in Kenya that had either merged or undergone acquisitions. The focus was on mergers and acquisitions that took place in the industry between 2008 and 2016.

3.3.2. Sample Design

Sampling design can be defined as a procedure or plan drawn up before any data is collected to obtain a representative from a given population. It is also known as sampling plan or survey design (Saunders, Lewis &Thornhill, 2016). The sampling frame, sampling technique and sample size, all make up the sample design.

3.3.2.1. Sampling Frame

A sampling frame is a list of elements from which a sample can be drawn (Zikmund et al., 2013). The study's sampling frame for the secondary data was the list of all merged financial institutions approved by the Central Bank of Kenya. At the time of the study, there were 33 mergers and 9 acquisitions from the period 1989 to 2016.

3.3.2.2. Sampling Technique

Sampling technique is the process of selecting several individuals for a study in such a way that they represent the large group from which they were selected from (Kothari, 2004). The study adopted a purposive quantitative sampling method. The main goal of purposive sampling is to focus on characteristics of a population that are of interest, which then guides the researcher to answer the study's research objectives.

3.3.2.3. Sample Size

A sample refers to a small representative unit or group that is derived from the study population (Mugenda A. & Mugenda O., 2013). The sample of this study was all commercial banks that head either merged or undergone acquisitions between 2008 and 2016 as shown on appendix II. This period was chosen as the sampling period because there were many merger activities that had taken place after the country had recovered from the 2007 Kenyan general elections.

3.4. Data Collection Method

Data collection refers to the process of gathering raw and unprocessed information that can be processed into meaningful information (Christensen, Johnson, Turner, & Christensen, 2011). A secondary data collection template was used to collect the data used in the study.

3.4.1. Secondary Data Collection Template

A secondary data collection template was used to collect data on ROA, ROE, CAR and MSI for the commercial banks that had merged or undergone acquisitions between 2008 and 2016 in Kenya as shown on appendix I. This data was then used to come up with a checklist that was used to measure each specific objective as shown on appendix I A, B and C. This information was obtained from the audited financial statements of the merged financial institutions. In the data collection checklist, the ratio of net income to total assets was used as a proxy for asset management, the ratio of net income to equity was used as a proxy for shareholders' equity, the ratio of capital to risk weighted assets was used as a proxy for financial stability and finally the market share index was used as a proxy for financial performance.

3.5. Research Procedure

This is a step-by-step sequence of activities or course of action (with definite start and end) that must be followed in the same order to correctly perform a task (Kombo & Tromp, 2011). The research study was conducted by first developing the research objectives, secondly by identifying the sample data, and thirdly by analyzing the data and making recommendations on the study.

3.5.1. Development of the research objectives

The general objective of the study was to determine the effects of mergers and acquisitions on the financial performance of commercial banks in Kenya. The study was guided by three specific objectives namely: to determine the effect of asset management on financial performance; to determine the effect of shareholder's equity on financial performance and to investigate the effect of financial stability on financial performance.

3.5.2. Identification of the sample data

To come up with a sample, one needs to determine the purpose of the data collection and what type of information is necessary to collect to meet that purpose (Creswell, 2009). To help achieve this, the study considered data sources that were reliable, accessible, relevant, suitable, adequate and recent. The sample of this study was all commercial banks that head either merged or undergone acquisitions between 2008 and 2016 as shown on appendix II. This period was chosen as the sampling period because of its relevancy as there were several merger activities that had taken place after the country

had recovered from the 2007 general elections in Kenya. Relevant permission was then obtained to conduct the study at the selected financial institutions.

3.6.   Data Analysis Methods

Secondary data, three years before and three years after the event was retrieved from audited financial statements, annual reports published by Central Bank of Kenya and the respective bank websites. Financial ratios: return on assets (ROA), return on equity (ROE), capital asset ratio (CAR) and market share index (MSI) were then obtained from the statements and annual reports of commercial banks under study. Descriptive, correlation and regression analysis were then used to establish the effect of the mergers and acquisitions on financial performance of commercial banks in Kenya. The dependent performance indicators were ROA, ROE and CAR while the independent variable was the MSI. These were used to answer the specific research objectives: to investigate effects of Mergers or Acquisitions on shareholder's value of commercial banks in Kenya; to determine the effect of shareholder's equity on financial performance of acquisitions or merged commercial banks in Kenya; to determine the effect of asset management on financial performance of acquisition or merged commercial banks in Kenya; to investigate effect of financial stability on financial performance of acquisition or merged commercial banks in Kenya. Statistical Package for Social Science (SPSS) version 21 software was then used to perform regression and correlation tests on the data collected.

3.7.   Chapter Summary

This chapter is a presentation of the research design used in the study. It describes the population, the sampling procedure and the data collection methods that were used in the study. The main instruments of research in the study were the audited financial statements from the sampled institutions. The data collected was then analyzed using Statistical Package for Social Sciences (SPSS) version 21 software. The analyzed data was then used to obtain the descriptive, correlation and regression analysis to establish the effect of the mergers and acquisitions on financial performance of commercial banks in Kenya. The findings as well as results are presented in the next chapter.

CHAPTER 4

4.0.   RESULTS AND FINDINGS

4.1.   Introduction

The general objective of this study was to determine the effects of mergers and acquisitions on the financial performance of commercial banks in Kenya. This chapter discusses the findings of the data collected in chapter three for the individual institutions under study. The chapter gives a summary results of all the institution, then discusses results of each specific objective as follows: effect of shareholder's value on financial performance of merged commercial banks; effect of asset management on financial performance of merged commercial banks in Kenya and effect of asset management on financial performance of merged commercial banks in Kenya

4.2.   General Information

This section contains the Mean (M) of return on equity (ROE), return on assets (ROA), capital asset ratio (CAR) and market share index (MSI)for each of the sampled bank in the study.

4.2.1. Kenya Commercial Bank Merger in 2010

Table 4.1 KCB and Savings and Loan Ltd Merger

KCB and Savings and Loan Merger (2010)									
		Pre- Merger Period			Merger Period	Post-Merger Period			
Institution	Measure	2007	2008	2009	Mean (M)	2010	2011	2012	2013	Mean (M)
KCB	ROA	3.1	3	3.57	**3.22**	5.17	4.98	5.2	5.5	**5.23**
	ROE	30.07	26.9	28.69	**28.55**	28.23	31.18	29.8	28.4	**29.79**
	CAR	13.61	15.45	14.82	**14.63**	23.16	20.69	22.7	22.5	**21.96**
	MSI	12.57	13.21	14.21	**13.33**	13.98	14.52	13.54	12.83	**13.63**
		2007	2008	2009	Mean (M)					
Savings and Loan Ltd	ROA	3.3	3.9	5.14	**4.11**					
	ROE	31.79	46.8	50	**42.86**					
	CAR	20.3	14.93	25.54	**20.26**					
	MSI	0.99	1.02	1.12	**1.04**					

Source: Data findings

Pre-merger ROA mean for KCB was 3.22 while Savings and Loan Ltd was 4.11, after the merger this rose to a mean of 5.23. ROE mean for KCB before the merger was 28.55 while that of Savings and Loan Ltd was 42.86, after the merger the mean ROE was at 29.79. CAR for KCB before the merger was 14.63 while Savings and Loan Ltd was 20.26, this rose to mean of 21.96. Pre-merger mean MSI index for KCB was 13.33 while Savings and Loan Ltd was 1.04. After the merger the value rose to 13.63 as shown on table 4.1.

4.2.2. Prime Bank Ltd Merger in 2008

Prime Bank pre-merger ROA mean was 1.70, this rose to a mean of 2.59 after the merger. Pre-merger ROE mean was at 16.09, which rose to a post-merger mean of 22.24. CAR had a mean of 14.51 before the merger which rose to mean of 15.34. MSI had a pre-merger mean of 1.97 that rose to 1.95 after the merger as shown on table 4.2 below.

Table 4.2: Prime Bank Merger in 2008

Credit Limited and Prime Bank Merger										
		Pre-Merger Period				Merger Period	Post-Merger Period			
Instituion	Measure	2005	2006	2007	Mean (M)	2008	2009	2010	2011	Mean (M)
Credit Ltd.	ROA	1.4	1.5	2.2	**1.7**	2.3	2.33	2.37	3.07	**2.59**
	ROE	17.32	14.51	16.45	**16.09**	15	18.09	19.74	28.88	**22.24**
	CAR	15.59	13	14.94	**14.51**	16.05	15.74	13.76	16.51	**15.34**
	MSI	1.71	2.24	1.96	**1.97**	2.31	2.41	1.8	1.64	**1.95**

Source: Data findings

4.2.3. CFC Stanbic Bank Ltd merger in 2008

The ROA mean for CFC Bank Limited before its merger with Stanbic Bank was 2.25 for CFC bank and 2.93 for Stanbic bank, these values were higher that the ROA mean after the merger which was at 1.85. Pre-merger ROE mean for CFC Bank was 21.88 and that of Stanbic Bank Kenya was 30.23. After the merger the value was at 22.69. CAR mean was 19.30 and 15.99 for CFC Bank and Stanbic Bank respectively, after the merger the mean value was 17.09. MSI pre-merger mean for CFC Bank was 3.64 and that of Stanbic bank was 3.54. After the merger the MSI mean rose to a mean of 5.49 as shown on table 4.3.

Table 4.3: CFC Bank Ltd and Stanbic Bank Ltd Merger

CFC Bank Ltd and Stanbic Bank (2008)										
		Pre- Merger Period				Merger Period	Post-Merger Period			
Instituion	Measure	2005	2006	2007	Mean (M)	2008	2009	2010	2011	Mean (M)
CFC Bank Ltd	ROA	1.54	2.1	3.1	**2.25**	1.5	1.35	1.96	2.23	**1.85**
	ROE	15.36	22.7	27.59	**21.88**	18.4	16.3	20.96	30.82	**22.69**
	CAR	20.48	18.29	19.13	**19.30**	14.65	16.04	16.2	19.04	**17.09**
	MSI	3.81	3.69	3.43	**3.64**	7.62	6.05	5.31	5.10	**5.49**
		2005	2006	2007	Mean (M)					
Stanbic Bank	ROA	2.5	2.9	3.4	**2.93**					
	ROE	21.64	33.48	35.57	**30.23**					
	CAR	16.31	17.63	14.03	**15.99**					
	MSI	3.01	3.90	3.70	**3.54**					

Source: Data findings

4.2.4. Jamii Bora Bank acquisition in 2010

Table 4.4 City Finance Bank (Jamii Bora Bank) Merger

Jamii Bora Bank Acquisition in 2010										
		Pre-Merger Period				Merger Period	Post-Merger Period			
Instituion	Measure	2007	2008	2009	Mean (M)	2010	2011	2012	2013	Mean (M)
City Finance Bank	ROA	-3.1	-0.5	-1.26	**-1.62**	-4.85	-1.79	1.5	1.3	**0.34**
	ROE	-8.74	-0.9	-0.02	**-3.22**	-8.19	-2.43	2.5	4	**1.36**
	CAR	77.93	78.27	94.28	**83.49**	35.69	110.5	83.6	25.8	**73.29**
	MSI	0.53	0.52	0.52	**0.52**	0.21	0.24	0.27	0.32	**0.28**

Source: Data findings

Before the acquisition in 2010 City Finance Bank Ltd, currently known as Jamii Bora Bank had a mean ROA of -1.62, this slightly rose to a mean of 0.34 after the acquisition. The ROE means before the acquisition was -3.22, which rose to 1.36 after the acquisition. The CAR mean was 83.49 which fell to 73.29 after the acquisition. MSI pre-merger mean was 0.52 which slightly fell to a mean of 0.28 after the merger as shown on table 4.4. above.

4.2.5. Equatorial Commercial Bank merged in 2010

Equatorial Commercial Bank pre-merger ROA mean was 0.96, while that of Southern Credit Banking Corporation was - 4.67, after their merger the value fell to a mean of - 1.03. Pre-merger ROE mean was 6.73 and 2.77 for Equatorial Commercial Bank and Southern Credit banking corporation respectively. After the merger the mean fell to a value of -24.60. CAR for Equatorial Commercial Bank before the merger was 20.71 while Southern Credit's mean was 9.46. After the merger CAR rose to a mean value of 11.82. Pre-merger MSI was 0.95 and 1.01 for Equatorial and Southern Credit respectively. This fell to 0.54 after the merger. These findings are shown below on table 4.5.

Table 4.5: Equatorial Commercial Bank and Southern Credit Banking Corporation Merger

Equatorial Commercial Bank Merger (2010)									
		Pre- Merger Period				Merger Period	Post-Merger Period		
Institution	Measure	2007	2008	2009	Mean (M)	2010	2011	2012	2013	Mean (M)
Equatorial Commercial Bank	ROA	1.4	-0.2	1.69	**0.96**	-0.32	0.55	-4.65	1.00	**-1.03**
	ROE	10.89	-1.2	10.51	**6.73**	-3.7	5.91	-90.8	11.1	**-24.60**
	CAR	20.29	21.07	20.77	**20.71**	14.49	14.27	8.9	12.3	**11.82**
	MSI	1.08	0.92	0.85	**0.95**	0.53	0.57	0.52	0.53	**0.54**
		2007	2008	2009	Mean (M)					
Southern Credit Banking Corporation	ROA	0.6	0.1	-14.7	**-4.67**					
	ROE	7.36	1.1	-0.15	**2.77**					
	CAR	16.86	15.6	-4.07	**9.46**					
	MSI	1.11	0.98	0.93	**1.01**					

Source: Data findings

4.2.6. K-Rep Bank acquisition in 2014

Centum Ltd acquired K-Rep bank in 2014. The bank is currently known as Sidian Bank. The ROA mean before the merger was 3.39 which fell to a value of 1.51 after the acquisition. The mean ROE before the acquisition was 23.05, this fell to a low of 7.57 after the acquisition. K-Rep had a mean CAR of 20.89 before the acquisition and 23.95 after. Pre-acquisition MSI was 0.45 and 0.60 after the acquisition as shown on table 4.6.

Table 4.6: K-Rep Acquisition

| | | K-Rep Bank Merger in 2014 | | | | | | | |
| | | Pre-Merger Period | | | | Merger Period | Post-Merger Period | | |
Instituion	Measure	2011	2012	2013	Mean (M)	2014	2015	2016	Mean (M)
K-Rep Bank	ROA	2.75	3.21	4.22	**3.39**	4.61	2.72	0.30	**1.51**
	ROE	19.23	20.1	29.81	**23.05**	29.98	13.54	1.60	**7.57**
	CAR	19.78	21.5	21.4	**20.89**	20.6	24.7	23.20	**23.95**
	MSI	0.47	0.42	0.47	**0.45**	0.51	0.60	0.60	**0.6**

Source: Data findings

4.2.7. Fina Bank acquisition in 2013

Fina Bank Limited was acquired by Guaranty Trust Bank Plc in 2013. The ROA mean before the acquisition was 1.73 which fell to a value of 1.49 after the acquisition. The mean ROE before the acquisition was 15.15, this fell to 6.98 after the acquisition. The mean CAR was 17.66 before the acquisition and 27.03 after the acquisition. Pre-acquisition MSI was 0.73 and 0.98 after the acquisition as shown on table 4.7.

Table 4.7: Fina Bank Acquisition

| | | FINA Bank merger in 2013 | | | | | | | |
| | | Pre-Merger Period | | | | Merger Period | Post-Merger Period | | |
Instituion	Measure	2010	2011	2012	Mean (M)	2013	2014	2015	2016	Mean (M)
FINA Bank	ROA	1.07	2.12	2.00	**1.73**	0.69	1.17	1.07	2.23	**1.49**
	ROE	11.32	20.22	13.9	**15.15**	4.06	7.43	5.6	7.90	**6.98**
	CAR	17.06	19.01	16.9	**17.66**	33.80	25.90	27.7	27.50	**27.03**
	MSI	0.76	0.69	0.74	**0.73**	1.09	1.07	0.97	0.90	**0.98**

Source: Data findings

4.2.8. Eco Bank acquisition in 2013

Kenya's East African Building Society (EABS) Bank was acquired by Ecobank Transnational Incorporated (ETI) in 2008. The ROA mean for EABS bank before the acquisition was 0.49 which fell to -1.99 after the acquisition. The mean ROE before the acquisition was 3.50, this fell to a value of 3.42 after the acquisition. The mean CAR

was18.58before the acquisition and 20.19 after the acquisition. Pre-acquisition MSI was 1.60 and 1.40 after the acquisition as shown on table 4.8.

Table 4.8: Ecobank and EABS Acquisition

Ecobank Kenya Ltd merger in 2008										
		Pre-Merger Period				Merger Period	Post-Merger Period			
Instituion	Measure	2005	2006	2007	Mean (M)	2008	2009	2010	2011	Mean (M)
EABS Bank	ROA	0.07	0.40	1.00	**0.49**	0.5	-7.13	0.7	0.45	**-1.99**
	ROE	0.56	3.01	6.94	**3.50**	3.8	-0.54	3.76	7.03	**3.42**
	CAR	16.97	20.55	18.23	**18.58**	15.52	15.67	19.33	25.58	**20.19**
	MSI	1.93	1.71	1.16	**1.60**	1.47	1.58	1.59	1.02	**1.40**

Source: Data findings

4.3. Effect of Asset Management on Financial Performance of Merged Commercial Banks in Kenya

Return on assets before and after the merger period was used to measure how the banks under study were managing their assets.

4.3.1. Descriptive statistics on Return on Assets

From the findings illustrated on table 4.9 there was a slight rise in the Mean (M) for return on assets from 1.3188 before merger to 1.3758 after merger. The Standard Deviation (SD) slightly fell from 3.34190 to 2.84065 after the merger. The variance (V) for return on assets also fell from 11.168 before merger to 8.069 after merger for the sampled banks.

Table 4.9 Descriptive statistics on ROA

	Mean (M)		Std. Deviation (SD)	Variance (V)	Skewness (S)	Kurtosis (K)
	Statistic	Std. Error	Statistic	Statistic	Statistic	Statistic
Pre-Merger	1.3188	0.58175	3.3419	11.168	-3.627	16.868
Post-Merger	1.3758	0.57985	2.84065	8.069	-1.348	3.027

4.3.2. Correlation Analysis Results of Return on Asset on financial performance

Results of the correlation analysis between performance and return on assets are illustrated in table 4.10. The results showed that there is a positive significant relationship between return on assets and performance $r(24) = .536, p < 0.01$.

Table 4.10 Correlation results of ROA

		ROA	Performance
ROA	**Pearson Correlation**	1	.536[**]
	Sig. (2-tailed)		.007
	N	24	24
Performance	**Pearson Correlation**	.536[**]	1
	Sig. (2-tailed)	.007	
	N	24	24

**. Correlation is significant at the 0.01 level (2-tailed)

4.3.3. Regression analysis on the effect of ROA on financial performance

Table 4.11 Pre-Merger ANOVA results of ROA

Model Summary				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.026[a]	0.001	-0.032	20.37043

a. Predictors: (Constant), ROA

Pre-Merger ANOVA					
Model		**Sum of Squares**	**df**	**Mean Square**	**F**	**Sig.**
1	**Regression**	8.531	1	8.531	0.021	.887b
	Residual	12863.59	31	414.955		
	Total	12872.121	32			

a. Dependent Variable: Financial Performance

b. Predictors: (Constant), ROA

	Coefficient				
	Unstandardized Coefficients	**Standardized Coefficients**			
Model	B	Beta	**t**	**Sig.**	
1 (Constant)	5.893		1.543	0.133	
ROA	0.155	0.026	0.143	0.887	

The goodness of fit model on table 4.11 shows regression results of pre-merger ANOVA between performance and return on assets. There was a significant effect on ROA: $F (2, 24) = 0.02$, $p = .89$. R2 value of 0.001 indicated that only 0.1% of the variations in financial performance are explained by return on assets. A coefficient of 0.026 signified that there was a weak relationship between performance and return on assets. This means that changes in one variable were not correlated with changes in the second variable.

Table 4.12 Post-Merger ANOVA results of ROA

		Model Summary		
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.536[a]	.287	.254	2.45285

a. Predictors: (Constant), ROA

		Post-Merger ANOVA[a]			
Model	**Sum of Squares**	**df**	**Mean Square**	**F**	**Sig.**
1 Regression	53.231	1	53.231	8.848	.0007[b]
Residual	132.363	22	6.016		
Total	185.594	23			

a. Dependent Variable: Performance

b. Predictors: (Constant), ROA

Model		Coefficient				
		Unstandardized Coefficients		**Standardized Coefficients**	**t**	**Sig.**
		B	Std. Error	Beta		
1	(Constant)	0.298	0.618		0.482	0.635
	ROA	0.347	0.117	0.536	2.974	0.007

a. Dependent Variable: Financial Performance

Regression results of post-merger ANOVA indicated a significance of $F (2, 24) = 8.48$, $p = 0.01$. An R2 of 0.287 indicated that28.7% of the variations in performance are explained by return on assets after the merger or acquisition event. The overall model is shown on table 4.12

4.4. Effect of Shareholder's Equity on Financial Performance of Merged Commercial Banks in Kenya

4.4.1. Descriptive Statistics on Shareholders' equity

Return on equity was used to measure shareholder's equity. Descriptive statistics were used to describe the pre-merger and post-merger values to determine if there were any changes and how this affected the performance of banks that had either merged or undergone acquisitions. There was a fall in the mean values for the return on equity from 17.0548 before merger to 9.6146 after merger. The standard deviation rose from 14.26795 to 24.12155 after the merger. The variance for return on assets also rose from 203.574 before merger to 581.849 after merger for the sampled banks as illustrated on table 4.13

Table4.13 Descriptive Statistics of Return on Equity

	Mean (M)		**Std. Deviation (SD)**	**Variance (V)**	**Skewness (S)**	**Kurtosis (K)**
	Statistic	**Std. Error**	**Statistic**	**Statistic**	**Statistic**	**Statistic**
Pre - Merger	17.0548	2.48373	14.26795	203.574	0.358	-0.276
Post - Merger	9.6146	4.92379	24.12155	581.849	-3.255	13.704

4.4.2. Correlation Analysis Results of Return on Equity on financial performance

Table 4.14 below shows the results of the correlation analysis between performance and return on equity. The results show that there is a positive significant relationship between return on equity and performance, *r (24) = .041, p<0.05.*

Table 4.14 Correlation results of ROE

		ROE	Performance
ROE	**Pearson Correlation**	1	.419[*]
	Sig. (2-tailed)		0.041
	N	24	24
Performance	**Pearson Correlation**	.419[*]	1
	Sig. (2-tailed)	0.041	
	N	24	24

* Correlation is significant at the 0.05 level (2-tailed).

4.4.3. Regression analysis on the effect of ROE on financial performance

Regression results of pre-merger ANOVA indicated that performance and return on equity had a significance $F (2, 24) = 0.133$, $p= 0.718$. An R2 of 0.004 indicates that only 0.4% of the variations in performance are explained by return on equity. The overall model significance is presented in Table 4.15.

Table 4.15 Pre-Merger ANOVA results of ROE

Model Summary				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.065[a]	0.004	-0.028	20.33377

a. Predictors: (Constant), ROE

Pre-Merger ANOVA[a]				
Model	**Sum of Squares**	**df**	**Mean Square**	**F**
Regression	54.79	1	54.79	0.133
1 Residual	12817.331	31	413.462	
Total	12872.121	32		

Coefficient				
Model	**Unstandardized Coefficients**	**Standardized Coefficients**	**t**	**Sig.**
	B	Beta		
1 (Constant)	7.661		1.376	0.179
ROE	-0.092	-0.065	-0.364	0.718

Regression results of post-merger ANOVA indicated a significance of $F(2, 24) = 4.69$, $p = 0.041$. An R2 of 0.176 indicated that 17.6 % of the variations in performance were explained by return on equity after the merger or acquisition event. The overall model is shown below on table 4.16. A coefficient of - 0.065 signified a negative correlation, meaning that an increase in performance resulted to a decrease on return on equity.

Table 4.16 Post-Merger ANOVA results of ROE

Model Summary				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.419[a]	.176	.138	4.06562

a. Predictors: (Constant), ROE

ROE Post-Merger ANOVA[a]					
Model	**Sum of Squares**	**df**	**Mean Square**	**F**	**Sig.**
1 Regression	77.524	1	77.524	4.690	.041[b]
Residual	363.644	22	16.529		
Total	441.169	23			

a. Dependent Variable: Performance

b. Predictors: (Constant), ROE

		Coefficient				
Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**t**	**Sig.**
		B	Std. Error	Beta		
1	(Constant)	2.372	.896		2.647	.015
	ROE	.076	.035	.419	2.166	.041

a. Dependent Variable: Post-Merger

4.5. Effect of Financial Stability on Financial Performance of Merged Commercial Banks in Kenya

Capital adequacy ratio before and after the merger period was used to measure financial stability of banks under the study.

4.5.1. Descriptive statistics on Capital Adequacy Ratio

Table 4.17 Descriptive Statistics of Capital Adequacy Ratio

	Mean (M)		**Std. Deviation (SD)**	**Variance (V)**	**Skewness (S)**
	Statistic	Std. Error	Statistic	Statistic	Statistic
Pre - Merger	23.2258	3.49101	20.05432	402.176	2.726
Post - Merger	26.1963	4.64439	22.75275	517.688	3.101

Source: Data findings

Findings illustrated on table 4.17 show that there was a rise in the mean values for the capital adequacy ratio from 23.2258 to 26.1963 after merger. The standard deviation also rose from 20.05432 to 22.75275 after the merger. The variance also rose from 402.176 before merger to 517.688 after merger.

4.5.2. Correlation analysis results of Capital Adequacy Ratio on financial performance

Results of the correlation analysis between performance and capital adequacy ratio are illustrated in table 4.18. The results showed that there was a significant negative correlation between capital adequacy ratio and performance, $r(24) = -0.178, p < 0.01$.

Table 4.18 Correlation results of CAR

		CAR	Performance
CAR	**Pearson Correlation**	1	-.178
	Sig. (2-tailed)		.405
	N	24	24
Performance	**Pearson Correlation**	-.178	1
	Sig. (2-tailed)	.405	
	N	24	24

**. Correlation is significant at the 0.01 level (2-tailed).

4.5.3. Regression analysis on the effect of CAR on financial performance

Table 4.19 Pre-Merger ANOVA results of CAR

Model Summary				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.085[a]	0.007	-0.025	20.3043

a. Predictors: (Constant), CAR

Pre-Merger ANOVA[a]

Model		Sum of Squares	df	Mean Square	F
	Regression	91.917	1	91.917	0.233
1	**Residual**	12780.205	31	412.265	
	Total	12872.121	32		

a. Dependent Variable: Financial Performance

b.Predictors: (Constant), CAR

Coefficients

Model		Unstandardized Coefficients	Standardized Coefficients	t	Sig.
		B	Beta		
1	(Constant)	8.06		1.477	0.15
	CAR	-0.085	-0.085	-0.472	0.64

Table 4.19 shows regression results of pre-merger ANOVA between performance and capital adequacy ratio. There was a significance of $F_{(2, 24)} = 0.23$, $p = 0.64$ and an R2 of 0.007 which indicates that only 0.07% of the variations in financial performance are explained by capital adequacy ratio. The overall model is shown below on table. A coefficient of -0.085 means that as one variable increases, the second variable decreases in value

Table 4.20 Post-Merger ANOVA results of CAR

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.178ᵃ	.032	-.012	4.40648

a. Predictors: (Constant), CAR

Post-Merger ANOVAᵃ

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	13.992	1	13.992	0.721	.405ᵇ
1	Residual	427.176	22	19.417		
	Total	441.169	23			

a. Dependent Variable: Performance

b. Predictors: (Constant), CAR

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.002	1.389		2.882	.009
	CAR	-.034	0.040	-.178	-.849	.405

a. Dependent Variable: Financial Performance

Regression results of post-merger ANOVA indicated a significance of $F_{(2, 24)} = 0.72$, $p = 0.405$. An R2 of 0.032 indicated that only3.2% of the variations in performance are explained by capital adequacy ratio after the merger or acquisition event. The overall model is shown on table 4.17. A coefficient of -1.78 shows a negative correlation and

implies that when there is an increase in performance then there is a decrease in capital adequacy ratio

4.6.   Chapter Summary

Return on assets in this study was used to measure asset management of commercial banks in Kenya. The results revealed a positive relationship between return on assets and performance *r (24) =.536, p < 0.01*. Regression results indicated that ROA explained 0.1% of the variance (R2=.01, *F (2, 24) = 0.02, p< 0.01*). This indicated that return on assets as a determinant of performance of Kenyan commercial banks positively influenced mergers and acquisitions. The more the mergers or acquisition institutions acquire assets, the better they perform.

Return on equity was used to measure the effects of mergers and acquisitions on shareholder's value of commercial banks in Kenya. The findingsrevealed a positive relationship between return on equity and performance, *r (24) = .041, p<0.05*. Results of the regression indicated that ROE is explained by 0.04% of the variance (R2 = .004, F (2, 24) = 0.133, p<.05). This implied that institutions that had either merged or undergone acquisition with higher shareholder's value also had a higher financial performance and hence a higher market share.

Capital adequacy ratio was used to measure the effect of mergers and acquisitions on financial stability of commercial banks in Kenya. There were inconsistent results regarding this variable. Findings showed a significant negative correlation of *r (24) =-0.178, p<0.01)*. Regression results indicated that CAR was explained by only 0.07% of the variance (R2=.007, F (2, 24) = 0.23, p<0.01). This means that the higher the capital adequacy ratio the institution has the lower the lower the financial performance of the institution.

CHAPTER 5

5.0. DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.1. Introduction

This chapter presents the summary of the study, discussion of the results and makes conclusions from the findings. Recommendations for improvement and further studies have also been discussed.

5.2. Summary

The general objective of this study was to determine the effects of mergers and acquisitions on the financial performance of commercial banks in Kenya. The study was guided by the following specific objectives: to determine the effect of shareholder's value on financial performance of merged commercial banks in Kenya, to determine the effect of asset management on financial performance of merged commercial banks in Kenya and to investigate effect of financial stability on financial performance of merged commercial banks in Kenya. The study adopted a descriptive research design which focused on determining the relationship between mergers and acquisitions and the financial performance of the commercial banks between 2008 and 2016.The population of the study consisted of financial institutions in Kenya that had either merged or undergone acquisitions from 2000 to 2016 as approved by the Central Bank of Kenya. The sample was selected using the purposive method which involved studying ten commercial banks that had merged between the years 2008 to 2016. Secondary data, three years before and three years after the event was retrieved from audited financial statements, annual reports published by Central Bank of Kenya and the respective bank websites. An analysis of the data was performed through use of the Statistical Package for Social Sciences (SPSS) version 21 software. Descriptive, correlation and regression analysis methods were used to establish the effect of the mergers and acquisitions on financial performance of commercial banks in Kenya.

Return on Assets in this study was used to measure asset management of commercial banks in Kenya. The results revealed a positive relationship between return on assets and performance *r (24) =.536, p < 0.01*. This meant that return on assets as a determinant of performance of Kenyan commercial banks positively influenced mergers and acquisitions. The more the mergers or acquisition institutions acquire assets, the better they perform. Return on Equity was used to measure the effects of mergers and

acquisitions on shareholder's equity of commercial banks in Kenya. The findings also revealed a positive relationship between return on equity and performance, *r (24) = .041, p<0.05*. This implied that institutions that had either merged or undergone acquisition with higher shareholder's value also had a higher financial performance and hence, a higher market share. Capital Adequacy Ratio was used to measure the effect of mergers and acquisitions on financial stability of commercial banks in Kenya. There were inconsistent results regarding this variable. Findings showed a significant negative correlation of *r (24) =-0.178, p<0.01*. Meaning that the higher the capital adequacy ratio the institution has, the lower the lower the financial performance of the institution.

5.3. Discussion
5.3.1. Effect of Asset Management on Financial Performance of Merged Commercial Banks in Kenya

Five out of the ten banks under study had a decrease in return on assets after the merger or acquisition event. The banks included CFC Stanbic Bank, Equatorial Commercial Bank, K-Rep Bank, Fina Bank and Ecobank. This could be an indication of failure by management to use its resources efficiently of the sampled banks. Descriptive results also indicated a slight rise in the mean values for return on assets from 1.3188 before merger to 1.3758 after merger. This signified that the companies were able to earn higher profits in relation to their overall resources after the merger or acquisition. Akenga and Olang (2017) presented a similar study on the effects of asset growth on financial performance of commercial banks. They tested the hypothesis that asset growth had no significant effect on financial performance using a t-test analysis. Asset growth was measured using change in value of assets which resulted to a significant value of 0.002 which was below the 0.05 significance level. The results led to the rejection of the null hypothesis that asset growth had no significant effect on financial performance of commercial banks

Results of the correlation analysis illustrated a positive significant relationship between return on assets and performance (*r (24) =.536, p < 0.01*). This meant that an increase in return from assets led to an increase in market share and consequently an increase on financial performance. Regression results of post-merger ANOVA ($R2=.28$, *F* (2, 24) = 8.48, *p<0.01*) indicated a P value of 0.007 which was less than the significant level of 0.05. A coefficient is said to be statistically significant only when its p-value is smaller than0.05. An R2 of 0.287 indicated that28.7 % of the variations in performance were

explained by return on assets after the merger or acquisition event. This value can be seen to be higher than that of ROE in relation to performance of this study. The coefficient of ROA though not statistical significant shows that as financial performance increases, the return on assets also increases.

Mugambi (2014) also conducted a similar study on the effect of mergers and acquisition on financial performance of commercial banks in Kenya. His study also found an increase in the mean return on assets after merger. This depicts that the post-merger period had higher performance than pre-merger period. Ndung'u (2010) also had similar results on the same study. His study resulted in an increase in the return on equity which was found to be statistically significant with a value of 0.000 which was less than P value of 0.05. From the findings on the t-test for the data on return on assets before and after merger, it was found that there was an increase in t value which indicated an increase in the return on assets as well.

5.3.2. Effect of Shareholder's Equity on Financial Performance of Merged Commercial Banks in Kenya

The findings indicated that the banks under study achieved a higher mean return on shareholder's equity after the event except for Equatorial Commercial Bank and K-Rep Bank. Descriptive results however indicated that there was a fall in the mean values for the return on equity from 17.0548 before the merger to 9.6146 after merger owing to the two banks whereby, one recorded a negative result, while the other had a decrease in the mean value after the merger. Similar studies have resulted into contradicting results for example Mugambi (2014) whose findings indicated an increase in mean return on equity after merger or acquisition depicted by an increase in the mean from 2.079 on pre-merger period to 3.965 on the post-merger period. The P value for ROE after the merger was 0.041, which was lower than the significant level of 0.05providing evidence that, the merger or acquisition was significant on the financial performance of commercial banks. The direction of the relationship was positive which signified that an increase in return on equity resulted to an increase on market share. Regression results of post-merger ANOVA indicated that regression between financial performance and return on equity was statistically significant with a P value of 0.41 being less than 0.05. An R^2 of 0.004 indicated that only 0.4% of the variations in performance were explained by return on

equity. Mailany (2014) carried out a similar study to establish the effect of mergers and acquisition on the financial performance of oil companies in Kenya. The study findings indicated that return on equity (ROE) mean decreased after the merger/acquisition. The study findings also observed that; the merger or acquisition processes in the oil industry in Kenya had affected the capital structure of the new companies by having additional shareholding which led to an increase in share equity of the merged/acquired firm thus reducing the return on equity. Regression results indicated that the null hypothesis was rejected since the calculated p value (0.007) was less than the critical P value of 0.05. Akenga and Olang (2017) conducted a similar study where they tested the hypothesis that shareholders value had no significant effect on financial performance using a t-test. The study had a significant value of 0.04 which was below the 5% significance level.

5.3.3. Effect of Financial Stability on Financial Performance of Merged Commercial banks in Kenya.

CFC Bank, Jamii Bora Bank and Equatorial Bank all recorded a decrease in their capital adequacy ratios after the merger or acquisition. Descriptive statistics show a rise in the capital adequacy ratio from 23.2258 to 26.1963 after merger or acquisition. Generally, a bank with a high capital adequacy ratio is safe and likely to meet its financial obligations. Ndung'u (2010) also found similar results on a similar study regarding mergers. His results revealed a statically significant relationship with an increase in the t value for capital adequacy ratio from 19.064 to 21.764. This was an indication that there was notable increase in financial leverage of the companies under study.

Correlation results between performance and capital adequacy ratio illustrated a significant negative relationship with a P value of -0.178. According to this study, this signified that a higher capital adequacy ratio would result to a lower financial performance of the institution. Regression results of post-merger ANOVA indicated a significance of 0.405. An R^2 of 0.032 indicated that only 3.2 % of the variations in performance explained capital adequacy ratio after the merger or acquisition event. Marembo (2012) also confirmed mixed reactions from a similar study that analyzed the effect of mergers and acquisitions on the capital adequacy ratio. The results indicated that some banks posted an increase in the capital adequacy ratio while others posted a decrease in the capital adequacy ratio for five years after the merger. An increase in the capital adequacy ratio confirmed that the banks were able to meet their liabilities and

other obligations when they were due, while a decrease in the capital adequacy ratio confirmed that the respective banks were not able meet their liabilities and other obligations when they were due.

5.4. Conclusion

5.4.1. Effect of Asset Management on Financial Performance of Merged Commercial Banks in Kenya

Regression results on return on assets had the highest variation explaining performance at 28.7 % after the merger event. Despite this, the banks under study had mixed results some recording an increase while others recording a decrease in return on assets after the merger or acquisition. Correlation results showed that there was a positive significant relationship between return on equity and performanceof institutions that had either merged or undergone through acquisitions.

5.4.2. Effect of Shareholder's Equity on Financial Performance of Merged Commercial Banks in Kenya

The findings on regression results showed that most of the sampled banks had an increase in return on equity after the merger or acquisition with a variation of only 0.4% explaining performance. Correlation results showed a significant relationship between financial performance and return on equity of institutions that had either merged or undergone through acquisitions.

5.4.3. Effect of Financial Stability on Financial Performance of Merged Commercial Banks in Kenya.

Descriptive results indicated that some banks posted an increase in the capital adequacy ratio while others posted a decrease in the capital adequacy ratio. Regression results indicated that only 3.2 % of the variations in performance explained capital adequacy ratio after the merger or acquisition event in the study. Correlation results showed no significant relationship between financial stability and financial performance of merged institutions.

5.5. Recommendations

5.5.1. Recommendations for improvement

5.5.1.1. Effect of Asset Management on Financial Performance of Merged Commercial Banks in Kenya

A low return on assets signifies that a company is not making adequate profits or is overinvested in assets that are not profitable. Management can work on reducing the bank's operational cost by downsizing facilities and by relocating to affordable premises. They can also sell off fixed assets that are not being used.

5.5.1.2. Effect of Shareholder's Equity on Financial Performance of Merged Commercial Banks in Kenya

Management should strive to efficiently utilize the shareholders' funds at their disposal. This will encourage the shareholder to invest more in the banks. The banks can increase return on equity by increasing the amount of debt capital relative to its equity capital, increase the overall bank's profit relative to its equity and reduce the excess cash on the balance sheet by paying out dividends it to its shareholders.

5.5.1.3. Effect of Financial Stability on Financial Performance of Merged Commercial Banks in Kenya.

An increase in the capital adequacy ratio confirms that a bank can meet its liabilities and other obligations as and when they are due and be able to absorb more losses in case of default loans bycustomers. To raise the capital adequacy ratio, banks can consider reducing the share of its profit by paying out in dividends, by issuing new equity such as through a rights issue to existing shareholders and finally by replacing riskier or more expensive loans with safer ones or government securities.

5.5.2. Recommendations for Further Studies

Further studies should be carried out on the effect of mergers and acquisitions on financial performance from time to time to establish trends for longer periods and to capture new opportunities that have recently emerged in Kenya. Since the study can use various variables to measure performance, both quantitative and qualitative variables should be included in the studies to come up with more comprehensive conclusions.

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APPENDICES

APPENDIX I: Secondary Data Collection Template

Period	Year	Financial Institution	ROA	ROE	CAR	MSI
Year 1						
Year 2						
Year 3						
Merger/Acquisition						
Year 1						
Year 2						
Year 3						

A. Effect of Asset Management on Financial Performance of Merged Commercial Banks in Kenya checklist

Financial Institution	ROA						
	Year 1	Year 2	Year 3	Merger	Year 1	Year 2	Year 3
KCB							
S&L ltd							
Prime Bank							
CFC Bank							
Stanbic							
Jamii bora							
Equatorial							
Southern Credit							
Sidian							
Guarantee Trust Bank							
Ecobank							

B. Effect of Shareholder's Equity on Financial Performance of Merged Commercial Banks in Kenya checklist

Financial Institution	ROE						
	Year 1	Year 2	Year 3	Merger	Year 1	Year 2	Year 3
KCB							
S&L ltd							
Prime Bank							
CFC Bank							
Stanbic							
Jamii bora							
Equatorial							
Southern Credit							
Sidian							
Guarantee Trust Bank							
Ecobank							

C. Effect of Financial Stability on Financial Performance of Merged Commercial Banks in Kenya checklist

Financial Institution	CAR						
	Year 1	Year 2	Year 3	Merger	Year 1	Year 2	Year 3
KCB							
S&L ltd							
Prime Bank							
CFC Bank							
Stanbic							
Jamii bora							
Equatorial							
Southern Credit							
Sidian							
Guarantee Trust Bank							
Ecobank							

APPENDIX II: List of Commercial Bank Mergers and acquisitions in Kenya from 2008 – 2016

Mergers

Institution	Merged with	Current Name	Date approved by CBK
Prime Capital & Credit Ltd	Prime Bank Ltd	Prime Bank Ltd	01.01.2008
CFC Bank Ltd	Stanbic Bank Ltd	CFC Stanbic Bank Ltd	01.06.2008
Savings and Loan (K) Limited	Kenya Commercial Bank Limited	Kenya Commercial Bank Limited	01.02.2010
City Finance Bank Ltd	Jamii Bora Kenya Ltd	Jamii Bora Bank Ltd	11.02.2010
Equatorial Commercial Bank Ltd	Southern Credit Banking Corporation Ltd	Equatorial Commercial Bank Ltd	01.06.2010

Acquisitions

Institution	Acquired by	Current Name	Date approved by CBK
EABS Bank Ltd	Ecobank Kenya Ltd	Ecobank Ltd	16.06.2008
Fina Bank Ltd	Guaranty Trust Bank Plc	Guaranty Trust Bank (Kenya) Ltd	08.11.2013
K-Rep Bank Ltd	Centum Ltd	K-Rep Bank Ltd	29.10.2014
Equatorial Commercial Bank Ltd	Mwalimu Sacco Society Ltd	Equatorial Commercial Bank Ltd	31.12.2014
Giro Commercial Bank Ltd	I&M Bank Ltd	I&M Bank Ltd	13.02.2016

Source: Central Bank of Kenya