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EFFECT OF DIVERSIFICATION ON THE FINANCIAL PERFORMANCE OF MERGED INSTITUTIONS

Dr. Agnes Ogada, Dr. George Achoki and Dr Amos Njuguna

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[1*] Dr. Agnes Ogada

Post graduate student, United States International University-Africa

***Corresponding Author's email: awuorogada@gmail.com**

[2] Dr. George Achoki

Lecturer, United States International University-Africa [3]
Dr. Amos Njuguna

Lecturer, United States International University-Africa

Abstract

Purpose: The purpose of the study was to assess the effect of diversification on the financial performance of merged institutions.

Methodology: The study adopted a mixed methodology research design. The study population included all the 51 merged financial service institutions in Kenya. Purposive sampling was used. Primary data was obtained from questionnaires and a secondary data collection template was also used. The researcher used quantitative techniques in analyzing the data. Descriptive analysis for the study included the use of means, frequencies and percentages. Inferential statistics such as correlation analysis was also used. Panel data analysis was also applied. Further, a pre and post merger analysis was used.

Results: Diversification had no significant effect on financial performance of merged institutions.

Unique contribution to theory, practice and policy: The study findings call for a re-assessment of the literature on diversification. Further research is necessary to study why sometimes the diversification-performance relationship is positive, others negative, and often quadratic. Further research is needed to investigate whether diversification effects on performance depends on the industries considered. This study recommends that companies with a weak and unstable capital base should seek to consolidate their establishments through mergers and acquisitions. Through mergers and acquisitions, these companies will be able to extend their market share and revenue base hence increase their profitability. In addition, mergers and acquisition leads to a higher CAR which improves the financial soundness of the companies.

Keywords: *diversification, financial performance, merged institutions.*

1.0 INTRODUCTION

1.1 Background of the Study

Mergers and Acquisitions is an important financial tool that enables companies to grow faster and provide returns to owners and investors (Sherman, 2011). According to Ross, Westerfield and Jordan (2003), a merger is the complete absorption of one firm by another, wherein the acquiring firm retains the identity and the acquired firm ceases to exist. Mergers and Acquisitions also refer

to the change in ownership, business mix, assets mix and alliance with the view to maximizing shareholders' value and improve the firm performance (Pazarkis, Vogiatzoglo, Christodoulou, Drogalas, 2006;Gaughan,2012;Nakamura, 2015). According to (Pazarkis *et al*, 2010;Gaughan,2012;Nakamura, 2015), one of the main elements of improving company performance is the boom in mergers and acquisitions. A merger is a corporate strategy usually done between two or more companies where by the acquiring firm and the acquired firm stands on a merger agreement.

Due to changes in the operating environment, several licensed institutions have had to merge or one institution takes over another's operations (Hitt, Ireland & Hoskissn, 2009;Fluck and Lynch, 2011). Some of the reasons put forward for mergers and acquisitions are: to gain greater market power, gain access to innovative capabilities thus reducing the risks associated with the development of a new product or service, maximize efficiency through economies of scale and scope and finally in some cases, reshape a firm's competitive scope (Hitt *et al*., 2009;Fluck et al,2011; Vermeulen and Bakerma, 2011; Vaara, 2012). Other reasons include short-term solution to finance problems that companies face due to information asymmetries (Fluck*et al*2011), revitalize the company by bringing innew knowledge to foster long-term survival (Vermeulen *et al* 2011) and to achieve synergy effects (Lubatkin, 2007; Vaara, 2012).

The synergistic effect of mergers and acquisitions includes economies of scale through greater output, avoidance of duplication of facilities and staff services and stronger financial base. The economic benefits as a reason for pursuing a merger or an acquisition include income enhancement, cost reduction and growth (Amedu, 2014). Some of the reasons for mergers and acquisitions are to: purchase a company having competent management; improve earnings per share, inject fresh ideas for better prospects and enhancement of shareholders' wealth, gain access to the financial market, eliminate duplicate and competing facilities, secure scarce raw materials, diversify into other products or markets or to complete a product range, greater asset backing; and enhance economy of scale and corporate growth (Akinsulire, 2012: Amedu, 2014).

Many merger and acquisition are undertaken with the belief that a merged firm may operate more efficiently than two separate firms. A firm can obtain cost reductions in several ways through a merger or an acquisition (Ross *et.al* 2003). According to Motis (2007), a firm can obtain cost advantage when its average cost per unit decreases as the total level of output increases.Economies of vertical integration can be gained by combining the companies operating in the same industry. For example, airline companies have purchased hotels and car rental companies. Vertical integration of companies may have a significant impact on companies to reduce cost, to improve supply chain operations, and in increase the profit margin. Some companies may acquire another company for the sake of complementary resources which makes the products commercially viable. For example, according to (Motis 2007) a winter clothing store could merge with a summer clothing store to produce more sales over both the winter and summer seasons.

1.2 Problem Statement

The resultant benefits and costs of mergers and acquisitions is a strategic issue which may impact positively or negatively on financial performance (Healy, Palepu and Ruback 2012). Shareholders and their agents are therefore faced with a problem of trying to ascertain whether this strategic decision and activity will result in improvement of better financial performance (Katuu, 2003). Mergers and acquisitions could also concern policy makers because they may have negative

consequences on the competitive environment by creating monopolies (Wang 2007). Several economic theories and M&A literature support the idea that shareholders experience positive abnormal returns arising from expected value creation post-merger (Halebian, 2009;Cartwright et al, 2013; Moeller et al., 2015). Thus, M&As are expected to create value as a result of firms exploiting economic resources that are both available and implementable but, the general result is that the shareholders of target firms earn positive and significant returns, whereas returns for acquiring firms are much lower and possibly negative(Cartwright *et al*, 2013). This is the practical gap that necessitates this study.

Many studies in M&As have been done in developed markets globally mainly in Asia, Europe and the USA. Healy,*et al* (1992) examined post-acquisition performance for 50 largest U.S. mergers between 1979 and 1984 by measuring cash flow performance, and concluded that performance of merging firms improved significantly following acquisitions, when compared to their respective industries. Lubatkin (1983) reviewed the findings of studies that investigated either directly or indirectly the question, "Do mergers provide real benefits to the combined firm?" The review suggested that combined firms might benefit from merging because of technical, and diversification synergies. Ghosh (2001) examined the operating cash flow performance improvement after corporate acquisitions; and the results showed that merging firms did not show evidence of improvements in the operating cash flow performance of postmerger and acquisition. Wang (2007) investigated the wealth effect of investment banks and fairness opinions they provide in corporate mergers and acquisitions. The study found that firms undertaking opinioned mergers under-perform firms with non-opinioned matching mergers in short windows around the announcement date. Lack of conclusiveness of studies linking merging activity to performance is a distinct knowledge gap.

Limited studies have been carried out on the M & As in the Kenyan market. These studies' findings have not shown that M & A activities positively affect financial performance. Some of them even give contradictory findings. Chesang (2002) carried out a studied on implications of merger restructuring on performance of commercial banks in Kenya. She used ratio analysis on this study and concluded that there was improved performance in some cases though; the extent of the contribution was not significant. Korir (2006) researched on the merger effects of companies listed in the NSE and found out that mergers improve performance of companies listed at the NSE. Ochieng (2006) did research on the merger between CBA & FABK and the results showed a decline in earnings and lower ratios arising out of the deal. Marangu (2007) studied effects of mergers on financial performance of non-listed banks in Kenya from 19942001 and using the ratio analysis, he concluded that there was significant improvement in performance for the non-listed banks that merged compared to the non-listed banks that did not merge within the same period. The empirical studies conducted in Kenya including; (Maranga, 2010; Katuu, 2003; Muya, 2006; Kiplagat, 2006; Wesonga, 2006; Nyagah, 2007; Njoroge, 2007; Kithinji, 2007, Ndura 2010, Ndung'u 2011, and Ireri 2011) have all failed to treat mergers and acquisitions as a strategic activity. Despite these M&As activities continue to take place in the Kenyan economy; this presents a conceptual knowledge gap. In light of these inconclusiveness and conceptual gaps poised from these past studies, this study sought to establish if mergers and acquisitions strategic activities lead to improved financial performance of financial services institutions in Kenya

1.3 Research Objective

The objective of this study was to assess the effect of diversification on the financial performance of merged institutions.

2.0 LITERATURE REVIEW

2.1 Theoretical Review

2.1.1 Diversification Theory

Firms pursue diversification for a variety of reasons; it may be driven by increasing demand from managers and employees to diversify, it may also be pursued in order to preserve organizational and reputational capital, or it can be sought for financial and tax advantages and mergers can also be pursued to reduce risk (Crawford &Alchian, 1978). While shareholders can diversify in the industry, employees have limited options to diversify their labor income sources. Therefore, diversification in the firm can provide managers and other employees with job security and opportunities for promotion, and other things being constant, this can lead to lower labor costs.

Further, in modern theory of the firm, employees usually acquire and accumulate knowledge that is specific for the firm and which cannot be used elsewhere. However, when the firm is liquidated the knowledge streams that had been created are destroyed and this resource is lost. Diversification ensures that there can be a smooth and efficient transition of the firm's knowledge to other business activities hence helping in the continuity of the firm (Campa and Kedia, 2002). Firms can achieve diversification either through internal growth or mergers. However, mergers are preferred because firms quite often lack internal growth opportunities due to lack of resources or when there is excess capacity in the industry.

Amihud and Lev, (1999); Lane and Canella, (1998); Lubatkin, (1999); Denis, (1999), intimate that the firm's choice to diversify is considered a major strategic decision. There is a clear distinction between portfolio diversification and firm growth and the two should be treated as such; however in most literature; researchers recognize diversification as the key driver for firm growth. Hence diversification is seen as a form of growth marketing strategy by which firms can enter new industries, products, services and even markets (Williamson, 1975). Given this scenario; then growth is seen to be an incentive for firms to diversify (Panzar and Willig, 1981).

Although, diversification is considered as a key driver for the firm's growth and as a strategic decision, studies by (Morck, Shlefier and Vishny, 1990; Denis, 1999) show that the costs of diversification far outweighs the benefits. It may therefore appear that diversification may negatively affect the firm's value.Primarily; the negative effects of diversification are that characteristics of firms that diversify may cause them to be discounted (Campa et al, 2002). (Berger and Ofek 1995, Servaes 1996, and Lang and Stulz 1994) support this view by showing that diversified firms trade at a discount compared to non-diversified firms in the same industry.

These results seem to hold true for different time spans and regions; so, there is a growing theoretical consensus that the discount on firms with a diversified portfolio implies a destruction of value that may be the result of diversification.(Campa et al, 2002) support the view that this diversification strategy does not seem to maximize shareholders value. The diversification discount has since caused firms to be more focused in the composition of their activities. Studies conducted by Bhagut, Shleifer and Vishny (1990), Liebeskind and Opler (1992), Berger*et al* (1995) and comment and Jarrel (1995), state that focused corporate strategies lead to higher market value and higher stock returns; which is contrary to diversifying firms, that may experience loss of comparative advantage because they are not primarily focusing on their core activities (Denis, 1999).

Despite the arguments for by (Williamson, 1975; Panzar et al, 1981) and against by (Morck*, et al,* 1990; Denis, 1999) the effects of diversification strategy on firm performance, it is important to point out that stock price movements should not have anything to do with increase or decrease in firm risk. The reason being that, all gains from firm diversification should have already been achieved by stockholders (Capital Asset Pricing Model). So, according to the Capital Asset Pricing Model (CAPM), shareholders can decrease their investment risk by applying diversification to their own portfolio (Teece, 1982).In a theoretically considered perfect world without taxes and transaction costs, free information, riskless bargaining and lending and rational utility maximizing agents, diversification will not affect firm value. Based on these assumptions and the argument made by Teece (1982), it is plausible to expect that a diversification strategy would not have an effect on firm performance.

2.2 Empirical Review

Diversification refers to a firm's entry into a new market. It means the increase by a firm in the kinds of businesses which it operates, being that diversity either related to products, geographical markets or knowledge (Chandler, 2010;Berger *et al*., 2010;Clarke, 2011; Chartejee and Wernerfelt, 2012). Diversification seeks to minimize credit and other risks and to reduce volatility in profits. It is achieved through merger by expanding geographically and by taking on different products or developing new ones using newly-acquired capability. Diversification is often the main driver of cross-sector conglomerates and cross-border mergers (Berger *et al*., 2010).

Managers of firms often give diversification as a reason for entering into mergers and acquisitions. The explanation behind this is that the risk of earnings volatility is minimized when the activities of a firm are diversified. Thus when one aspect of operations is on the downside the loss can be compensated for or offset by increased or continued earnings in another aspect. This will then smoothen the earnings a company, which over time leads to smoothening of the stock price of a company; hence giving investors more confidence to invest in it. Diversification is also seen as a risk reduction function of mergers;(Brealey et al, 2013), have though described this as dubious reason for mergers; this is so because though diversification in itself is a good thing there is need to analyze the cost associated with the venture as opposed to other options. According to Brealey *et al* (2013), diversification is easier and cheaper to the individual shareholder than for the corporation. Thus while diversification may shield a company against a downturn in an industry it does not deliver value. This is because individual shareholders are able to achieve the same cushion by diversifying their individual portfolios at much lower costs than those of mergers. Indeed research suggests that in most cases diversification does not increase the firm‘s value. In fact many studies find that diversified firms are worth significantly less than the sum of their individual parts.

Companies diversify in order to broaden their activities by increasing services, markets and products. Thus the aim of diversifying is to enable firms enter other business units that are different from their core activities; however diversification strategy in itself does not exist in a single form. (Amit, 2011, Lyon et al 2012, John et al 2010). Argue that most literature conducted on diversification are in agreement that diversification is a form of growth strategy. Many organizations implement two or more forms of growth strategies, in order to speed up the increase in market share or sales thereby improving financial performance of firms (Jacquemin et al, 2009). Previously diversification came either accidentally or by intuition and diversifying into unrelated business (conglomerate) according (Mueller 2010) was a way to decrease the risk involved in the existing operations of the business. Montgomery (2014) identifies three primary reasons that drive

companies to implement diversification strategies. *First* is market–power belief which assumes that as a firm becomes a conglomerate, it can obtain stronger position. *Second*is the agency attitude; this assumes that managers implement diversification to uplift status of the firm and also reduce risk of financial volatility in times of economic turbulence. *Third*is the resource based view that encourages firms to diversify when it has excess resources; these resources may be utilized elsewhere to improve the firms' productivity.

Ansoff (1957) first articulated diversification strategy by stating that diversification means a new product development or new market entry; and since then, diversification has always been associated with entering a new industry or field (Rumelt, 1982). . According to (Rumelt 1982), the market power view expresses that if a firm keeps operating in a single business, then after some time it becomes unprofitable. (Montgomery, 2014) states that agency view proposes that if diversification is pursued to fulfill management desires and not maximization of profit, then it will ultimately bring the performance levels down. Based on theresource based view perspective, Rumelt's (1982) research indicated that firms who were able to leverage skills and resources among other activities were able to achieve optimum performance results as compared to those firms who did not share anything.

3.0 RESEARCH METHODOLOGY

The study adopted a mixed methodology research design where qualitative and quantitative research approaches were used to answer the research questions. The study population included all the 51 merged financial service institutions in Kenya which had completed their merger process by 31 December 2013. Purposive sampling was used. Primary data was obtained from questionnaires and a secondary data collection template was used to collect data on Return on Assets, Return on Equity and mergers and acquisitions aspects. The researcher used quantitative techniques in analyzing the data. Descriptive analysis for the study included the use of means, frequencies and percentages to describe the primary and secondary data collected. Inferential statistics such as correlation analysis was also used to test for the relationship of the variables from the secondary data. Panel data analysis was also applied to describe change in the study variables over time and trends over a period of five years from 2009 to 2013. A pre and post merger analysis was used to test whether the merger and acquisitions had brought any significant difference in the merged firms.

4.0 RESULTS AND DISCUSSIONS

4.1 Response Rate

Table 1 shows the response rate. **Table 1: Response Rate**

Response	Frequency	Percent
Returned	83	69.2%
Unreturned	37	30.8%

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Total 120 100%

Out of which 83 were properly filled and returned, representing a response rate of 69.2% as shown on table 1. According to Mugenda and Mugenda (2013) and also Kothari (2010) a response rate of 50% is adequate for a study. Babbie (2004) also asserted that return rates of 50% are acceptable to analyze and publish, 60% is good and 70% is very good.

4.2 Demographic Characteristics of Respondents who participated in the Primary Study. Table 2 below presents the results for the demographic characteristics of the respondents.

Table 2: Demographics Demography

Category	Frequency	Percent		
Gender	Female		36	43.4
	Male		47	56.6
	Total		**83**	**100**

Age	20-30	17	20.5
	31-40	22	26.5
	41-50	23	27.7
	Above 51	21	25.3
	Total	**83**	**100**
department	Accounts/Finance	25	30.1
	HR	6	7.2
	Customerservice/Business Development/Relationship Management	11	13.3
	Operations/strategy/planning	17	20.5
	Credit/risk/debt recovery	18	21.7
	Asset Finance	6	7.2
	Total	**83**	**100**
Position	Top Manager	15	18.1
	Senior Manager	25	30.1
	Middle Manager	43	51.8
	Total	**83**	**100**
Academic Qualification	College	14	16.8
	Undergraduate	37	44.6
	Masters	32	38.6
	Total	**83**	**100**
Number of Employees	11-50 employees	29	34.9
	over 50 employees	54	65.1
	Total	**83**	**100**

Majority of the respondents were male who represented 56.6 % of the sample while 43.4% were female. On the question of age, 20.5% the respondents were in the age bracket of between 2030years, 25.5 % were between 31-40 years, 27.7% were between 41-50 years while 25.3% were above 51 years. On the question on department, 30.1% of the respondents worked in the finance/account departments, 7.2% were from the HR department, 13.3% of were from the Customer service/Business Development/Relationship Management departments, 20.5% were from the operations, strategy and planning departments, 21.7% of the respondents were from the Credit, risk and debt recovery departments and 7.2% were from asset finance department.

The respondents were also requested to indicate their current position they held in the different departments 51.8% which was the majority indicated that they were in middle management position, 30.1% were in senior management position while 18.1% of the respondents indicated that they held top management positions.

On the question of academic qualification 44.6% had undergraduate qualification, 38.6% had masters qualification, while only16.89% had a college qualification. Lastly the respondents were requested to indicate the number of employees in their institutions, 65.1s% who were the majority indicated that their institution had over 50 employees

The respondents stated that the mergers took place through the replacement of inefficient managers of the acquired firms and amalgamations. The respondents cited gaining market share, competitive advantage, increasing revenues, risk and product diversification and improving shareholder value were stated as the most important motivating factors behind the merger and acquisition. The most obvious motive to engage in M&A was to obtain synergy effects. These were attained through cost savings gained from economies of scale and scope.

On the question of the critical strategies that the management put in place to enhance success of the merger and acquisition, respondents stated size of merging partners, number of bidders and methods of financing. Stocks were preferred as a financing method. Majority of the respondents responded in the affirmative that the pursuit of cost efficiency, diversification, synergy, strategy and board size had succeeded since the merger and acquisition had brought about increase in profitability and economies of scale, increase in sales operations, increase in value of assets and board membership.

4.3 Description of Merged Financial Institutions

4.3.1 Diversification

Results in table 3 below indicate the descriptive statistics of diversification from the secondary data collected. Diversification was defined as the number of branches.

Table 3: Descriptive Diversification

Variable	Year	Observations	Mean	Std. Dev.	Min	Max
Diversification	2009	40	22.275	36.8837	2	149
	2010	40	23.6	40.0262	1	165
	2011	40	24.075	38.7361	2	161
	2012	41	26.5366	40.558	2	166
	2013	41	28.7073	44.4186	2	182
Average			**25.0388**	**40.1245**		

The mean diversification for the period 2009to 2013 ranged between 22.2 and 28.7, with the standard deviation ranging between 36.8 and 44.4indicating significant variability in diversification over time.

Figure 1 shows the diversification trend for the merged institutions from the year 2009 to 2013.

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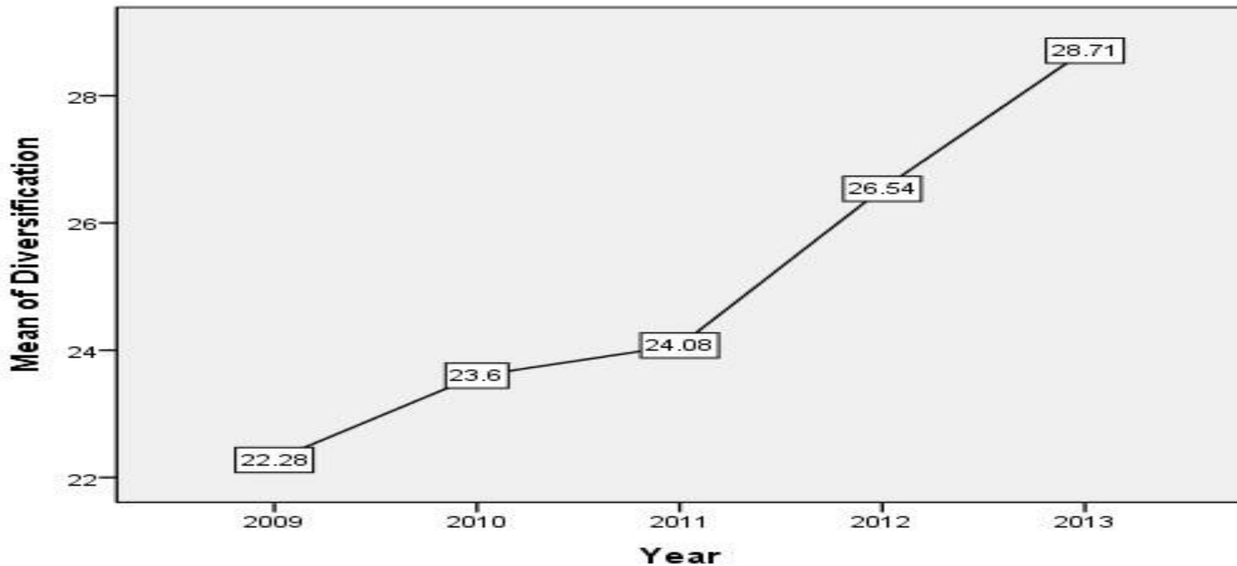

Figure 1: Diversification Trend

The trend indicates that diversification has been rising through the years.

4.4 Effect of Diversification on Financial Performance (secondary)

4.4.1 Correlation Analysis Results on the effect of Diversification on Financial Performance (Secondary)

Table 4 presents the results of the correlation analysis between diversification measured as the number of branches, ROA and ROE.

Table 4: Correlation Analysis (Diversification)

		ROA	ROE	Diversification
ROA	Pearson Correlation	1	.410**	-0.063
	Sig. (2-tailed)		0.00	0.37
ROE	Pearson Correlation	.410**	1	-0.063
	Sig. (2-tailed)	0.00		0.376
Diversification	Pearson Correlation	-0.063	-0.063	1
	Sig. (2-tailed)	0.37	0.376	

The results show that there is a negative non-significant relationship between ROA, ROE and diversification (r=-.063, p=-0.371), (r=-.063, p=0.376).

4.4.2 Regression Analysis on the effect of Diversification on Financial Performance

Regression analysis was conducted to empirically determine whether diversification was a significant determinant of performance which is measured in ROA and ROE.

Table 5: Regression Analysis (Diversification)

	ROA	ROE
Parameter estimate	Coefficient(P value)	Coefficient(P value)
Constant	0.237 (0.015)	.148(0.000)
Diversification	-.002(0.370)	.000(.376)
R Squared	0.004	0.004
F statistic (ANOVA)	1.097 (0.370)	.005(0.376)

Regression results in Table 4.17 indicated the goodness of fit for the regression between diversification and ROA is 0.004. An R squared of 0.004 indicates that only 0. 4% of the variations in ROA are explained by diversification. The overall model significance is also presented in Table 5. The overall model of ROA was not significant with an F statistic of 1.097.The overall model of ROE was not significant with an F statistic of .005.

The regression equation is therefore:

ROA= 0.237-0.002 Diversification.

4.4.3 Hypothesis Testing

To determine whether diversification had an impact on the performance of merged financial institutions, the hypothesis that there is no significant relationship between diversification and financial performance of merged institutions was tested.

Decision rule: reject hypothesis if calculated p value is less than the critical p value of 0.05

Regression results in Table 5 indicate that the null hypothesis is not rejected since the calculated p value (0.370/0.376) is more than the critical p value (0.05). Therefore, there is no significant relationship between diversification and financial performance of merged institutions.

4.4.4 Pre and Post Merger Analysis

To test whether there is a statistical difference in diversification mean before and after merger, an event window analysis was carried out.

Table 6: Diversification Pre and Post Merger Analysis

		Merger	Std.	Error	Sig. (2period	Std. N	Mean T
					Deviation		Mean tailed)
Diversification/Number of Branches	1	23	13.26	5.376	9.401	1.96	0.00
	0	45	4.47	4.282	4.11	0.613	0.00

Results in Table 6 below indicate that, there is a significant statistical difference in diversification mean before and after merging. This implies that merging lead to an increase in the total number of branches.

4.4.5 Effect of Diversification on Financial Performance (Primary Data)

The study used primary data to explain the effect of diversification on financial performance of merged institutions. The responses were rated on a likert scale and the results presented in Table 7.

Table 7: Descriptive analysis for diversification (primary data)

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	Std. Devn
1. Our institution has established many branches as a result of merger and acquisition activity	6.0%	20.5%	8.4%	34.9%	30.1%	3.6	1.3
2. New branches formed after the merger have resulted into an the expansion market portfolio	3.6%	7.2%	6.0%	53.0%	30.1%	4.0	1.0
3. New branches formed after the merger has led to an increase in product portfolio	8.4%	8.4%	4.8%	45.8%	32.5%	3.9	1.2
4. New branches formed after the merger has led to an increase in investment portfolio	4.8%	9.6%	7.2%	49.4%	28.9%	3.9	1.1
5. New branches formed after the merger has attracted a wide human resource portfolio	2.4%	16.9%	3.6%	42.2%	34.9%	3.9	1.1
Average						**3.9**	**1.1**

Majority (65%) of the respondents agreed that their institution had established many branches as a result of merger and acquisition, 26.5% disagreed while 8.4% reserved their opinion. Most of the respondents (83.1%) agreed that new branches formed after the merger had resulted into the expansion market portfolio, 6% were neutral while only 10.8% disagreed. On the question on whether new branches formed after the merger had led to an increase in product portfolio, majority

of the respondents (78.3%) agreed, 4.8% reserved their opinion while 16.8% disagreed. Seventy eight percent (78.3%) of the respondents agreed that new branches formed after the merger has led to an increase in investment portfolio, 7.2% reserved their opinion while 14.4% disagreed. Finally, majority of the respondents (77.1%) of the respondents agreed to the statement that new branches formed after the merger has attracted a wide human resource portfolio, 3.6% reserved their comment while 19.3% disagreed. On a five point scale, the average mean of the responses was 3.9 which means that majority of the respondents were agreeing to the statements in the questionnaire; however the answers were varied as shown by a standard deviation of 1.1.

4.4.6 Comparative Analysis of Effect of Diversification on Financial Performance Table 8shows a comparison on the effect of diversification on ROE in the insurance and banking sectors.

Table 8: Effect of Diversification on ROE

	Banks	**Insurance**
Parameter estimate	Coefficient(P value)	Coefficient(P value)
Constant	0.142(0.000)	0.136(0.000)
Diversification	0.008 (0.509)	0.002(0.277)
R Squared	0.004	0.015
F statistic (ANOVA)	4.309 (0.509)	1.198 (0.277)

From the table, diversification had no significant impact on performance in either the banking industry or the insurance sector.

Table 9: Effect of Diversification on ROA

	Banks	**Insurance**
Parameter estimate	Coefficient(P value)	Coefficient(P value)
Constant	1.04(0.005)	0.014(0.489)
Diversification	0.264(0.029)	0.17(0.117)
R Squared	0.40	0.30
F statistic (ANOVA)	4.895(0.029)	2.511(0.117)

Table 9 shows that diversification was a significant determinant of ROA in the banking sector (r=0.264, p=0.029) but not in the insurance sector.

The regression model for the banking sector is therefore: ROA= 1.04+0.264 diversification

5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 Conclusions

A test was conducted on the effect of diversification on financial performance. There is no significant relationship between diversification and financial performance of merged institutions. The study however revealed that the merged financial institutions had has established many branches as a result of merger and acquisition activity, new branches formed after the merger has attracted a wide human resource portfolio, new branches formed after the merger has led to an increase in product portfolio, new branches formed after the merger has led to an increase in investment portfolio and that new branches formed after the merger have resulted into the expansion market portfolio. The implication is that a high degree of diversification seems to exist in merged financial services institutions

5.2 Recommendations

In the sample of mergers studied, there is evidence that an investor should not be jittery to invest in the companies that are planning to acquire another because the market fundamentals do not significantly change. This leads to assertion that that the merging companies are mature, and they could have undertaken these mergers to gain a new product or region to continue to perform at growing company levels. Therefore, future mergers should be pegged on the benefits to be realized from the post-merger synergies

This study recommends that companies with a weak and unstable capital base should seek to consolidate their establishments through mergers and acquisitions. Through mergers and acquisitions, these companies will be able to extend their market share and revenue base hence increase their profitability. In addition, mergers and acquisition leads to a higher CAR which improves the financial soundness of the companies

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