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The Impact of Merger and Acquisition on Firm Performance in East Africa

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Abstract:
Purpose: The purpose of this study was to establish the impact of merger and acquisition (M&A) on firm performance in East Africa.
Methodology: We employed an event study to calculate the cumulative abnormal returns to evaluate M&A performance and shareholder wealth. We also used accounting ratio - Return on Equity to evaluate firm performance. Our dataset consists of 330 observations of 234 M&A deals that occurred in a period of 2005 to 2015, using secondary data of publicly listed firms on the various East African States stock exchange markets. All the data used was obtained from Zephyr for the deals and the stock values data was from Thomson one database (DataStream).

Findings: We find that mergers and acquisitions are significantly associated with firm performance. Results further indicate that M &A announcements generate significant abnormal returns to the firm's shareholders and also, there is a positive relationship between the domestic M&A deals and firm performance. Further, there is a positive relationship between cross boarder M & A deals and firm performance and domestic merger and acquisition deals perform better than the cross border M&A deals in improving firm performance.

Originality: The research gives an insight on how domestic Merger and Acquisition deals perform relative to cross border M&A deals in East Africa and how merger and acquisition can improve firm performance. The East African region has recently had some of the fastest growing M&A activities on the African continent. Thus, this study contributes to the existing literature on the effect of merger and acquisition on firm performance using evidence from the entire East African region. Further, this study is of value to the East African Community in regards to evaluating its objectives on regional economic growth through M&A influence and also driving positive business and logical decisions on M&A activities in the East African region.
Paper type: Research Paper
Keywords: Merger, Acquisition, East Africa, Firm performance

1.Introduction and motivation

In this study, we report the impact of merger and acquisition on firm performance in East Africa which has some of the fastest growing Merger & Acquisition activities on the African continent. The East African region encompasses some of the fastest growing and most sophisticated economies in Africa with Kenya in the lead in Merger and Acquisition activities (KPMG, 2014). Kenya has experienced considerable increase in M&A activities with over 134 transactions sealed from the

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year 2010 to 2016. The formation of Competition Authority of Kenya (CAK) under the Competition Act Cap 504 laws of Kenya is associated with inspiring growth in M&A activities in the country (Inoti, Onyuma and Muiru, 2014). Scholars like Ismail et al. (2010) found that some measures of corporate performance such as profitability suggest statistically significant gains in the years following Merger and Acquisition while Ferreira et al (2014) indicated that, mergers and acquisitions are important approaches through which firms carry out their domestic and international strategies and have been noted as the Chief Executive Officers' ideal strategy of improving firm performance.

Firm performance has been a major focus of various stakeholders including the academicians in the recent past given that the level of competition has gone to another level (Ismail et al., 2010; Lakstutiene, Stankeviciene, Norvaisiene and Narbutiene, 2015; Nkundabanyanga, 2016) and thus the need for studies of this nature to provide solutions for improvement of firm performance especially in the African context. Prior studies indicate various explanations of firm performance among these is included board governance and intellectual capital (Nkundabanyanga, 2016; Nkundabanyanga et al., 2014), acquisitions (Lakstutiene, et al., 2015) and mergers (Tao, Liu, Gao and Xia, 2016; Ndung'u, 2011; Akben-Selcuk and Altiok-Yilmaz, 2011; Wanguru, 2011; Vennet, 1996; Delaney and Wamuziri, 2004), inventory management (Koumanakos, 2008), bribery (Williams, Martinez-Perez and Kedir, 2016), board structure (Bhatt and Bhattacharya, 2015), and learning capability (Goh, Elliott and Quon, 2012). In their study, Serra and Ferreira (2010) identified four pillars of improving firm performance and these include; leader and top management team, strategic focus, trust in the future and resources support.

The firm's motivation for mergers and acquisitions is for various reasons with realization that business combinations provide an opportunity to create new value to the economic and wealth for their shareholders (Krishna and Paul, 2007). This new value can be created through taking advantage of the economies of scale that can be achieved through a combination as a result of the new firm performing a function more effectively and efficiently more than the two separate firms. The value would also be increased by combining firms with complimentary resources for efficiency and effectiveness in the business operations. Bender and Ward (2009) indicated that, companies require to grow in order to generate capital gains for their shareholder(s)' wealth increase and to justify the growth value already priced into their shares. One way company growth can be achieved is through merger and acquisition process. Accordingly, many companies look to mergers or acquisitions as a means to obtain the appropriate growth within the required time frame. Merger and acquisition performs a vital role in corporate finance through enabling firms to achieve different set objectives and financial strategies. In East Africa, firms have been merging with the aim of improving financial performance. This study thus aims to establish the impact of M & A on firm performance in East Africa given that the East African region has recently had some of the fastest growing Merger &Acquisition activities on the African continent. An event study methodology covering 234 M&A deals was employed and results indicate a significant relationship between M&A and firm performance. This study's results further indicate that M &A announcements generate significant abnormal returns to the firm's shareholders and also, there is a positive relationship between the domestic M&A deals and firm performance. Further, there is a positive relationship between cross boarder M & A deals and firm performance and domestic merger and acquisition deals perform better than the cross border M&A deals. Similar results were observed in earlier studies, for instance, in their study, Kumar and Bansal (2008) found out that there is a significant impact of mergers and acquisitions (M & As) on corporate performance in India. Further, Delaney and Wamuziri, (2004) indicated that the abnormal returns for target firms increase noticeably in two days before the announcement of a bid for M&A. Delaney and Wamuziri (2004) results further show that there was a significant increase in trading volume and share price of all target firms studied prior to the announcement of a take-over bid. Similarly,

Hossain, Heaney and Koh, (2016) and Ghosh and Lee, (2000) found out that acquiring firms with no director trading and firms with net director purchases in the 12 months prior to the M&A announcement earn positive abnormal returns. Likewise, Ndung'u (2011) studied the effects of merger and acquisitions on financial performance of commercial banks in Kenya and found that there was an improvement in financial performance after the merger. However, Wanguru (2011) reported negative results in regards to financial performance of firms after the merger where firm performance in some firms declined immediately after the merger but gradually improved in the next two years.

This study makes important contributions in the following ways. First, the exact mechanism through which firms can improve their performance especially during the time of recession is found. In the presence of an opportunity to merge or even acquire another firm, firms may explore this and survive in the future. Second, since there is limited literature on the effect of M&A on firm performance in the East African countries, this study becomes important in terms of its literature contribution to the already existing literature. Finally, this study is of value to the East African Community in regards to evaluating its objectives on regional economic growth through M&A influence and also driving positive business and logical decisions on M&A activities in the East African region.

The structure of the paper is as follows. Section 2 looks at the literature review and hypotheses' development. Section 3 provides methodology. The results are indicated in Section 4, while Section 5 discusses findings and finally section 6 is summary and conclusion.

2. Literature Review

Merger is an arrangement where the assets of two companies become vested in or under the control of one company which may or may not be one of the original two companies, which has all or substantially all, the shareholders of the two companies (Weinberg and Blank 1979). Gaughan (2002) opined that a merger is a combination of two companies in which only one company survives and the merged company ceases to exist, and the acquiring company assumes the assets and liabilities of the merged company.

M&A and financial performance

A number of studies have been conducted on M&As and how they affect firm performance (see Lakstutiene, et al., 2015; Tao, Liu, Gao and Xia, 2016; Ndung'u, 2011; Akben-Selcuk and Altiok-Yilmaz, 2011; Wanguru, 2011; Vennet, 1996; Delaney and Wamuziri, 2004; Rani, Yadav and Jain, 2015). In their study, Rani, Yadav and Jain (2015) who studied financial performance analysis of mergers and acquisitions in India found out a significant improvement in the profitability of the acquiring firms after the M&A period. Rain et al., (2015) further found that cash flows also improve after M&A. Ismail et al. (2010) found that measures of corporate performance such as profitability suggest statistical significant gains in the years following Merger and Acquisition. Similarly, Ndung'u (2011) conducted a study on the effects of merger and acquisition on financial performance using evidence obtained from the sixteen banks that underwent merger and acquisition in Kenya between 1999 and 2005 and found that there was an improvement in financial performance after the merger. Further, Wanguru (2011) carried out a study on the effect of mergers on profitability of firms in Kenya focusing on firms that had a merger between 2004 and 2008 and her observations were that, some of the merged companies' financial performance declined in the post-merger period, others had displayed better profitability in the post-merger after the merger. Kilelo (2013) concluded that banks venture into merger and acquisition in order to boost the capital base, market niche and returns to the investment and finally as an avenue to enter into the industry.

Studies such as Berger and Humphrey (1992), Shaffer (1993), and Focarelli and Panetta (2003) suggest that mergers have the potential to produce positive results in terms of improved financial performance due to synergetic benefits. Ali and Gupta (1999) examined 45 pairs of successful takeovers of listed firms that occurred in Malaysia during the period 1980 through 1993 and found that bidder firms achieved larger size at the expense of reduced profits both for themselves and the target firms. Ali and Gupta (1999) also found that the bidder firms in Malaysia have lower profitability, higher risk and lower leverage. Using data covering a period between 2000 and 2001, Fauzias and Mohamed (2003) found that mergers do not contribute to any significant increase in technical efficiency of commercial banks in Malaysia. This finding is supported by the results produced by Fauzias et al. (2005) who concluded that there is no significant difference between the pre- and post-merger period levels of efficiency for the ten anchor banks between 1995 and 2000. Using a sample of eight anchor banks from 1997 to 2002, Mahmood and Mohamad (2004) find that even though the bank mergers in Malaysia are "forced" in nature, it contributed to synergistic benefits and had a significant post-merger improvement based on four accrual operating performance measures. Mantravadi and Reddy (2008) studied the impact of merger on the operating performance of acquiring firms in India using several profitability ratios and debt/equity ratio, and the results indicated that there were some differences in terms of impact on operating performance following mergers in various industries in India. Kioko (2013), had a case study on mergers and acquisition as an entry strategy by CFC Stanbic bank in the Kenyan market and found that the merger enabled the bank to penetrate into the Kenyan market.

There has been extensive studies that provide possible explanations as to why a company would decide to participate in M&A other than performance. The most mentioned motive is to create value through synergy. However, there are many other reasons such as incorporating new technologies, expanding to new markets or even management self-interest, among others (Vazirani, 2012). Speculative motivations for mergers and acquisitions are relatively many but most significantly mergers and acquisition activities are started to generate effective and financial synergies that can, in turn, raise corporate growth, increase profitability, and improve shareholders' wealth (DePamphilis, 2011). Houston, James & Ryngaert (2001) and Delong (2003) stated that synergies are considered important determinants of shareholders' wealth creation. Equally, M&A institute investment activities and consequently the net additional cash flow present value made from these investment decisions should be positive. In contrast, Finkelstein, Cary & Sydney (2007) reject that creating greater value for acquiring shareholders, self-confidence and agency are the only valid motives for M&A. Finkelstein et al. (2007) argue that the reason that most M&A deals are considered as failures is because those motives fall short when explaining the real objectives behind M&A. Finkelstein et al. (2007) propose motivation categories: exploitation which includes the synergies, exploration, stasis and survival. Finkelstein et al. (2007) recognize reasons such as, assembling a long term industry position, exploring new potential markets, acquiring technologies and ideas for future growth, political favors, preventing competitors from presenting a threat in the future, size as defense against takeovers and preserving or maintaining customer and supplier relations. In Africa, there are studies that have reported a negative or no effect of the relationship between M&A and firm performance in the short run. Mushdzhi & Ward (2004) reports that South African acquiring firms' shareholders lost approximately 0.55% which was significant around the announcement dates. Smit and Ward (2007) used a sample of 27 firms listed on Johannesburg Securities Exchange (JSE) and found that acquiring firms in the same country neither earns significant positive abnormal returns nor negative abnormal returns in the short run. Barde and Salisu (2015)'s study that was conducted on Nigerian banking industry observed that merger and acquisition announcements have no impact on shareholder wealth in the short run. Gugler et al. (2003) examined and evaluated the effects of mergers and found that profitability is positive in all five years after mergers and is significant in every year at 10% level. On country level,

the results suggest that the United States, the United Kingdom, Continental Europe, Australia, New Zealand and Canada have the same pattern regarding the increase in profits and decrease in sales (Gugler et al., 2003). In Japan, the results were somewhat different as three of the five profit comparisons were negative, while sales were greater than analyzed in two of the five post- merger years (Gugler et al., 2003). Studies have reported losses after merger event which suggest negative effect of merger on performance for example Pazarskis et al (2006) reported a decreased profitability of firms due to M&A; Yeh and Hoshino (2002) found insignificant negative change in productivity, significant downward trend in cost effectiveness, significant negative effect on the sales growth rate, and downsize in the workforce after mergers and generally concluded that mergers have a negative impact on firm performance; Akben-Selcuk and Altiol-Yilmaz (2011) confirming negative impact of mergers on performance found that Return on Asset, Return on Equity and Return on Sales values are significantly lower than pre-acquisition value. Studies such as Ravenscraft and Scherer (1987) and Tambi (2005) also report negative impact of M&A on performance. Kumar (2009) concluded that the post-merger profitability, assets turnover and creditworthiness of the acquiring companies, on average, show no improvement when compared with premerger values. King et al. (2004) showed that M&A do not lead to superior financial performance. King et al. (2004) argued that M&A has a modest negative effect on long-term financial performance of acquiring firms. Cabanda and Pajara-Pascual (2007) reported that pre-merger and post-merger values attained mixed results. Some measures of corporate performance such as total assets turnover, which measures firms' efficiency, suggest statistically significant gains in the long run analysis following M&A. Other performance variables such as net income return on asset (ROA), return on sales (ROS), capital expenditure, capital expenditure/sales (CESA) and capital expenditure/total asset (CETA) did not show significant gains after merger in the short run analysis and thus established that merger does not lead to all improved corporate performance both in short-run and long-run period. In a recent study, Bhabra and Huang (2013) examined 137 M&A deals over the period from 1997 to 2007 which included Chinese public firms and found out that acquirers earned significant positive abnormal returns around the event announcement. In this study we try to reaffirm that:

HI(a): Merger and acquisition is associated with financial performance
HI(b): There is a positive abnormal return associated with M&A announcement for acquirer firms

Cross boarder acquisitions and domestic acquisitions

Cross Border M&As are driven by efficiency increase intentions. The main categories of efficiency gains are usually production rationalization, economies of scale and economies of scope as well as technological progress. Rationalization improvements might be significant for cross-border operations. Merging partners are more tending to diverge in their borderline manufacturing costs when they are originally positioned in separate nations, because of country inequalities in relation of capital and employment endowment, jurisdictional and official environment, among others. Also, they may take advantage from savings in business expenditures and a superior marketplace entry abroad (Bertrand & Zitouna, (2008). Ning et al. (2014) examined 335 Chinese cross border M&A samples during 1991 to 2010 and discovered significant positive abnormal returns for Chinese acquiring multinational enterprises. A similar result was also obtained by Tao et al. (2016) and their study looked into the short term stock performance of Chinese cross border acquirers on the event announcement in which findings were that, the announcement results attracted a positive stock market reaction and there was a negative relationship between the level of political risk and short run performance of Chinese listed bidders. However, many other studies report opposite

results, such as Chen and Young (2010)'s study where they used 39 cross border deals by 32 Chinese acquirers and found negative average cumulative abnormal returns around the announcement day. The results are supported by earlier studies of Aybar and Ficici (2009) who examine 433 cross border M&A deals by 58 emerging market companies including a significant proportion of Chinese firms. Primarily researchers have examined cross borders' short term abnormal returns as a performance measure (Bruner, 2004; correa, 2008). Some finance researchers have recently focused on acquirers' long term abnormal returns for example three years after the date of a cross border M&A announcement (Chakrabarti el al.2009; Mitchell and Stafford, 2000) and yet the results don't give definitive conclusions. For example, Seth et al. (2002) found that acquirers are more likely to create value by obtaining resources from foreign targets and yet less likely to create value due to managers' actions to reduce their job risk. From the foregoing discussion, we then hypothesize that:

H2: Cross border acquisition generates more returns than domestic acquisitions

Control variables

The works of Bartov, Gul and Tsui (2000) recommend controlling for confounding variables to avoid falsely rejecting the hypothesis which in fact should have been accepted. For this reason, we control for leverage, firm size and method of payment. Literature suggests that target shareholders are winners while acquiring firm shareholders are not as fortunate; bidders at best break even, but often lose during acquisitions resulting in significantly negative abnormal returns (Weidenbaum &Vogt, 1987; Bruner, 2004). However, the announcement stock based deals are associated with negative returns to the acquirer's shareholders whereas cash deals are close to zero or even slightly positive (Bruner, 2004). We make no predictions with regard to the impact of leverage on firm performance as the optimal debt level is likely to differ substantially on firm basis for example Haniffa & Hudaib (2006) showed in contrast to Weir et al (2002) a significant positive relationship between market performance and Leverage. Based on a sample of 12023 acquisitions from 1998 to 2001, researchers such as Moeller, Schlingemann & Stulz (2004) find strong evidence of a size effect in acquisition announcement returns. They argue that small public firms frequently undertake small acquisition resulting in small dollar gains that is shareholders of small firms earned roughly $9 billion during (1980-2001) time period, whereas large public firms frequently undertake large acquisitions resulting in large dollar losses that is shareholders of large firms lost roughly $312 billion during the (1980-2001) time period.

3. Methodology

Data description

To determine the impact of M&A on firm performance in East Africa, this study used data from zephyr for data concerning M&A deals in East African countries that is Kenya, Uganda, Tanzania, Rwanda, Burundi and South Sudan (East African Community) and the financial data has been taken from Thomson one Data Stream regarding stock prices and country's market index return. The Dataset contains data from 2005 to 2015 period, the acquirer and target firm must be listed. The target firms must be in East Africa and the acquirer firm can be from any part of the world (Cross boarder M&A) or East Africa (Domestic M&A). Firms whose data is completely unavailable were excluded.

The original dataset that meets the sample requirements consists of 330 observations of which only 234 were completed M&A deals in East Africa and almost three quarters of these mergers took place in Kenya and the rest in Uganda, Tanzania and Rwanda (Nairobi Securities Exchange (NSE), Rwanda stock Exchange (RSE), Uganda Securities Exchange (USE), Dar es Salaam Stock Exchange (DSE)); Burundi and South Sudan were excluded since they have no data available and the firms are not

publically traded or listed firms. Due to missing data for relevant variables the samples used for the analysis are smaller than the number of observations in the original database.

Table I reports the year and the number of M&A deals both domestic and cross border M&A event of publicly listed firms in East Africa of a period 2005 to 2015 which are included in our study. There was a positive spike in 2008 in the number of deals most especially the cross border M&A deals. Nevertheless, the total number of deals in East Africa both Cross Border M&A deals and Domestic M&A deals have increased from 16 to 30 deals from 2005 to 2015 of the publicly traded firms, this is attributed to the conducive political, social and economic climate of the East African states.

Table I: Distribution of Cross border and Domestic Merger and Acquisition deals in East Africa by year (2005-2015)

Year	*Cross-border deals*	*Domestic deals*	*Total number of deals*
2005	9	7	16
2006	9	4	13
2007	9	12	21
2008	21	8	29
2009	8	8	16
2010	11	3	14
2011	13	3	16
2012	14	1	15
2013	16	11	27
2014	26	11	37
2015	22	8	30
Total	***158***	***76***	***234***

Note: In the table above, the cross border deals mean the M&A deals where the acquirer is not a firm in the East African Community member state whereas the domestic deals represent M&A deals where the acquirer is a firm in the East African member state. The deals involve only publically listed firms in a period of 2005-2015.

Research design

We first use Event study to determine the behaviour of stock prices around the M&A announcement dates. Event study methodology is a widely used method to determine the effects of M&A's on stock price behaviours (Brown and Warner, 1980). The impact will be measured by Cumulative Abnormal Returns (CARs) during the Event window. A positive CAR suggests that M&As have a positive impact on firm performance and a negative CAR implies a negative impact on the firm performance.

In this study the abnormal stock returns are determined for both the acquirer and target firm. This is possible as one of the initial selection criteria was that both the target and acquirer firms were required to be listed. Standard Event Study methodology (Brown and Warner 1980) is used and the event window consists of three days (following Moeller and Schlingemann, 2005). A small event window is chosen because the most statistically reliable evidence on whether mergers create value for shareholders comes from traditional short-window event studies (Andrade et al. 2001). This is because a small event window reduces the chance that other effects influence the stock Price. Abnormal returns are calculated as illustrated below;

End of day, daily stock price ***(P_it)*** for each merger and acquisition event/firm ***i*** at the time ***t*** for the 137-day data period (-120, 40) which were obtained from DataStream. Daily returns ***(R_it)*** will be computed by taking the log of stock price (Strong, 1992)

$$R_{it} = ln \frac{P_{it}}{P_{i,t-1}}$$

Data during the estimation window is used to estimate the following market model specification (Brown and Warner, 1985; Strong, 1992) for each event / firm ***i.***

$$R_{it} = \alpha_i + \beta_i R_{mt} + \varepsilon_{it}$$

Where R_{mt} is the return on market index at time ***t,***

Expected returns during the testing period (R_{it}) will be calculated by:

$$\hat{R}_{it} = \hat{\alpha}_i + \hat{\beta}_i \hat{R}_{mt}$$

Where α_i and β_i are the estimated values of α_i and β_i. Abnormal returns for the testing period will be calculated as the difference between actual returns during the testing period and their forecasted values (based on the coefficients estimated during the estimation period);

$$AR_{it} = R_{it} - \hat{R}_{it}$$

$$CAR_i = \sum_{t=t_1}^{t_2} AR_{it}$$

CAR; Cumulative Abnormal Returns

t_2***;*** number of days in the event window

$AR_{it;}$ Abnormal returns of a firm for a day **t**

Significance tests are procedures used to verify the truth of the null hypothesis. In this study, the null hypothesis is that the abnormal returns at the announcement date and the ***CARs*** around the announcement date are different from zero and has an impact on return of the acquiring or acquired firm.

Model

We used two regression models to analyse the relationship between the size, leverage, Method of payment, M&A and Firm performance.

Model I

The dependent variable is firm performance and is determined by the cumulative abnormal returns (CAR) for acquiring firms during the (-1,1) event window as widely used in event studies such as Braggion et al. (2012). The higher the value of CAR the higher the excess returns earned by the acquiring firms' shareholders (Bruner, 2004). The regression equation we used for model I was to analyse the relationship between the predictor variables and firm performance using CAR as follows;

$$CARit = \alpha_0 + \beta_1 ACQit + \beta_2 CB_{it} + \beta_3 Method\ of\ payment_{it} + \beta 4 TDA_{it-1} + \beta_5 SIZEit-_{1} + \varepsilon it$$

Where; CAR_{it} is the cumulative abnormal return of firm i in year t for the 2005-2015 window.

The independent variables are determined as follows: ***ACQ*** is Acquirer / target and it's a dummy variable where 1 is for the acquirer and 0 is for the target, ***CB*** is also a dummy variable where 0 is for cross border M&A (between another country and an East African community member state) while 1 is for domestic M&A deals (between East African community member states)

The control variables are: ***Method of payment*** is another dummy variable where payment in shares equals to 1 if the deal was financed only by issuing shares to target shareholders and 0 otherwise, ***TDA***

is Leverage and we measure leverage as the ratio of total debt to total net assets of the firm and ***SIZE*** is firm size. We define firm size as the natural log transformation of the firm's book value of total assets. Finally, εit is an error term reflecting other factors that influence $\boldsymbol{CAR_{it.}}$

Model 2

The dependent variable is firm performance and is determined by return on equity (ROE), the shareholders' economic interest is best served when the ROE is high. We used the equation below to analyse the relationship between the various variables and firm performance.

$$\boldsymbol{ROE_{it-1} = \alpha_0 + \beta 1 ACQ_{it} + \beta_2 CB_{it} + \beta_3 TDA_{it-1} + \beta_4 SIZE_{it-1} + \varepsilon it}$$

Where;

$\boldsymbol{ROE_{it}}$-1 is the Return on Equity of the firm in the year before the Merger and Acquisition was announced. It's the firm's fiscal year net income after preferred stock dividends but before common stock dividends divided by shareholder's equity book value excluding preferred shares.

The independent variables are determined as follows;

ACQ is a dummy variable where 1 is for the acquirer and 0 is for the target.

CB is also a dummy variable where 0 is for cross border M&A (between another country and an East African community member state) while 1 is for domestic M&A deals (between East African community member states)

The control variables are:

TDA and we measure leverage as the ratio of total debt to total net assets of the firm.

SIZE is firm size and we define firm size as the natural log transformation of the firm's book value of total assets.

Finally, $\boldsymbol{\varepsilon it}$ is an error term reflecting other factors that influence $\boldsymbol{ROEi_{t-1}}$.

Table II: Variable operationalization in our research study

Global variable	Dimensions	Acronym	Operationalization	Data Source
Dependent variable				
Firm performance	Cumulative Abnormal returns	CAR3	CAR for firms with the (-1,1) event window of the announcement date of the M&A deal.	Thomson one DataStream (stock price and market index)
	Return on Equity	ROE	It is the firm's fiscal year net income after preferred stock dividends but before common stock dividends divided by shareholder's equity book value excluding preferred shares.	Thomson one DataStream
Predictor variables				
	Acquirer/ Target	ACQ	ACQ is a dummy variable where 1 is for the acquirer firms and 0 is for the target firms.	Zephyr database
	Cross border/ domestic deals	CB	CB is also a dummy variable where 0 is for cross border M&A while 1 is for domestic M&A.	Zephyr database
Control variables				
	Firm size	SIZE	The natural log transformation of the firm's book value of total assets.	Thomson one DataStream
	Leverage	TDA	The ratio of total debt to total net assets of the firm.	Thomson one DataStream
	Method of payment	Method of payment	Dummy variable where payment in shares equals to 1 if the deal was financed only by issuing shares to target shareholders and 0 otherwise .	Zephyr database

Descriptive statistics of firm performance (CAR3 regression)

Table III indicates that on average, acquiring firms tend to experience positive abnormal returns around the announcement date and an average of 74% of firms are Acquirer firms of which 40.9% of the firm sample dataset are domestic M&A deals. With regard to the control variables; the acquirers favour majority of other methods of payment over share/stock while the average rate of leverage is 77.7% and firms are relatively large. The variables all seem to be relatively normally distributed, low standard deviations and plausible minimum and maximum value numbers. In the total number of observations, only 271 observations had cumulative abnormal returns. We therefore considered only those firms that had CAR for the period 2005 to 2015.

Table III: Descriptive statistics of M&A performance (CAR3)

Variable	Obs	Mean	Std. Dev	Min	Max
car3	271	.0100194.	0834887	-.5502695	.2397428
Acquirer/ Target(Acq)	271	.7453875	.4364492	0	1
Cross border/domestic(cb)	271	.4095941.	4926687	0	1
leverage(tdat1)	271	.77758211	.259593	-8.158082	10.62585
sizet1	271	6.748257	1.565328	1.653213	10.49908
methodofpayment~t	271	.0516605	.2217502	0	1

Note: The table above presents descriptive statistics for the whole sample. The sample consists of 271 observations of publicly traded acquiring firms and target firms covered in zephyr and Thomson one database for a period of 2005 to 2015. All M&A firm deal is included provided the firm is publicly traded: **Dependent variable;** CAR3 for the event window (-1,1). Independent variables; ACQ is a dummy variable where 1 is for the acquirer and 0 is for the target. CB is also a dummy variable where 0 is for cross border M&A while 1 is for domestic M&A. Control variables; Leverage (TDA)- we measure leverage as the ratio of total debt to total net assets of the firm. Firm size (SIZE) as the natural log transformation of the firm's book value of total assets. Method of payment is another dummy variable where payment in shares equals to 1 if the deal was financed only by issuing shares to target shareholders and 0 otherwise.

Descriptive statistics of firm performance (ROE)

As reported in Table IV, firms in our sample of 330 observations are characterized on average a positive ROE of 44.45% and an average of 73% of firms are Acquirer firms of which 45.7% of the firm sample dataset are domestic M&A deals. With regard to the control variables; the acquirers favour majority of other methods of payment over share/stock plus while the average rate of leverage is 79.28% with relatively large firm size average. The variables all seem to be relatively normally distributed mean, low standard deviations and plausible minimum and maximum value numbers.

Table IV: Descriptive statistics of firm performance (ROE)

Variable	Obs	Mean	Std. Dev.	Min	Max
Return on Equity (roe1)	330	.4445187	1.048898	-3.462963	11.84106
Leverage (tdat1)	330	.7928554	1.192376	-8.158082	10.62585
size1	330	6.696163	1.639936	1.653213	10.49908
Cross border/domestic(cb)	330	.4575758	.4989535	0	1
Acquirer/target(acq)	330	.7272727	.4460381	0	1

Note: The table above presents descriptive statistics for the whole sample. The sample consists of 330 observations of publicly traded acquiring firms and target firms covered in zephyr and Thomson one database for a period of 2005 to 2015. All M&A firm deal is included provided the firm is publicly traded: Dependent variable; ROE is the firm's fiscal year net income after preferred stock dividends but before common stock dividends divided by shareholder's equity book value excluding preferred shares. Independent variables; ACQ is a dummy variable where 1 is for the acquirer and 0 is for the target. CB is also a dummy variable where 0 is for crossborder M&A while 1 is for domestic M&A. Control variables; Leverage (TDA) we measure leverage as the ratio of total debt to total net assets of the firm. firm size(SIZE) as the natural log transformation of the firm's book value of total assets.

4. Results

This part reports the results of our empirical analysis on the impact of M &A on firm performance. The event study t-statistics, correlation matrix analysis of M&A and firm performance, and the regression analysis results are presented.

Event study results

Variable	obs	Mean	Std.err	Std.dev	t-value	p-value
CAR3	271	.0100194	.0050716	.0834887	1.9756	0.0492

CAR3 denotes the 3day cumulative abnormal returns. T denotes for the t – statistics. CAR is significantly different from zero. Statistical significance at 10%, 5% and 1% level.

Table V: Cumulative Abnormal Returns (t-statistics)

Table V shows the event study results that represent a one-sample t-test at 95% level of confidence and the analysis of Cumulative Abnormal Returns around the announcement date to the merger and acquisition firms. Table V also represents the CAR3 and the t-statistics for the event window (-1, +1) which has 270 degree of freedom. The hypothesis is that M&A's announcements do not create wealth to the firm's shareholders that is CAR=0 while the alternative stated that M&A's announcement create wealth to the firm that is CAR ≠ 0. From Table V, the CAR3 has a t-statistics of 1.9756 with a p-value of 0.0492 which is significant at 5% level. We reject the null hypothesis and conclude that M&A announcements generate significant returns to the firm's shareholders.

Correlation matrix analysis of M&A performance

We ran the correlation matrix of the variables because it is an important indicator to measure the linear correlation and therefore it is used to measure collinearity problem between the variables. When the regression has a high multicollinearity, it may cause a high R-squared coefficient and the regression maybe statistically significant but the t-test of every parameter is not significant thus causing a different symbol of the regression coefficient and getting a completely wrong conclusion. From Table VI correlation matrix shows that there is a negative correlation between the M&A performance and the acquiring firms and a negative relationship between the method of payment (share deals) in M&A and return to investors. This means that investors prefer other methods of payment for example cash to shares. With regard to the other control variables leverage and size are positively correlated to M&A performance. There were no problem of multicollinearity, as the correlation coefficient are relatively low among the variables that is to say the coefficients do not exceed 0.80.

Table VI: Correlation matrix for M&A performance (CAR3)

	car3	**acq**	**cb**	**tdat1**	**sizet1**	**method~t**
car3	1.0000					
Acquirer/target(acq)	-0.0959	1.0000				
Cross border/domestic(cb)	0.0921	-0.7017	1.0000			
leverage(tdat1)	0.0584	-0.0016	-0.0324	1.0000		
sizet1	0.1527	-0.2323	0.3164	0.1463	1.0000	
methodofpa~t	-0.0465	-0.0167	0.1446	-0.0507	-0.0478	1.0000

Note; Significant at 1%, 5% and 10% level

Correlation matrix analysis of firm performance

The report from Table VII correlation matrix shows that there is a negative relationship between firm performance and the acquiring firms and a negative relationship between firm performance and the acquiring firm ROE though there is a positive relationship between the domestic M&A deals and firm performance. With regard to control variables leverage has positive relationship to firm performance and size has a negative relationship as reported in Table VII. There are no problems of multicollinearity, as the correlation coefficient are relatively low among the variables that is to say, the coefficients do not exceed 0.80.

	roe1	acq	tdat1	size1	cb
Return on Equity (roe1)	1.0000				
Acquirer/target(acq)	-0.0024	1.0000			
leverage(tdat1)	0.0945	-0.0245	1.0000		
size1	-0.0347	0.0083	-0.0540	1.0000	
Cross border/domestic(cb)	0.0381	-0.6667	0.0177	0.1494	1.0000

Table VII: Correlation matrix for firm performance (ROE)

Significant at 1%, 5% and 10% level

Regression analysis Results

Table VIII reports the results of the regression of model 1 that is the M&A performance determined by CAR. The CAR is negative with P-value significant at 10% level with a positive R-squared of 0.0305 making our regression significant for the relationship. The regression model estimates that the acquirer firms have a negative and significant relationship with CAR which indicates that we reject our second hypothesis which says; there is a positive abnormal return associated with a M&A announcement for acquirer firms. This means that for every acquirer after M&A there is a negative CAR coefficient of 0.0309. For the cross border M&A deals and Domestic M&A deals variable, the regression estimates show a positive and insignificant relationship with Cumulative abnormal returns which indicates that, for every domestic M&A deal, CAR increases with a coefficient of 0. 0042. This implies that the domestic M&A deals have a more positive M&A performance than the cross border M&A deals though it's not significant. From the regression results, the leverage (TDA) has a positive and insignificant relationship with the cumulative Abnormal Returns which indicates that, as leverage increases by 1%, the abnormal returns increase by 0.0025 though not significant. Firm size (SIZE) has a positive and 5% level of significant relationship with the cumulative Abnormal Returns (CAR) which indicates that as firm size increases by 1%, the abnormal returns increase by 0.0066978. The method of payment in our regression has a negative and insignificant relationship with cumulative abnormal returns which indicates that the majority of acquirer in our sample favour other methods of payment (cash) over stock based deals.

$$CARit = \beta 0 + \beta 1ACQit + \beta 2CBit + \beta 3Method\ of\ paymentit + \beta 4TDAit\text{-}1 + \beta 5SIZEit\text{-}1 + \varepsilon it$$

car3	Coef.	Std. Err.	t	P>t
Acquirer/target(acq)	-.0095732	.0012102	-7.91	0.080
Cross border/domestic(cb)	.0041811	.0019464	2.15	0.277
leverage(tdat1)	.0025543	.002736	0.93	0.522
sizet1	.0066978	.00019073	5.13	0.018
Method of payment	-.0161667	.0188853	-0.86	0.549
_cons	-.0309067	.0026906	-11.49	0.055
n	271			
R-squared	0.0305			

Table VIII: Regression Analysis (CAR3 – Firm performance)

Significant at 1%,5% and 10% level

$ROE_{it-1} = \beta 0 + \beta 1ACQ_{it} + \beta 2CB_{it} + \beta 3TDA_{it-1} + \beta 4SIZE_{it-1} + \varepsilon_{it}$

Return on Equity (roe1)	Coef.	Robust Std. Err.	t	P>t
Acquirer/target(acq)	.1215597	.01352828	.99	0.071
leverage(tdat1)	.0810694	.09198530	.88	0.540
size1	-.0266302	.011116	-2.40	0.252
Cross border/domestic(cb)	.162213	.009620916.86	0.038	
_cons	.395931	.012737731	.08	0.020
n	330			
R-squared	0.0130			

Significant at 1%,5% and 10% level

Table VII: Correlation matrix for firm performance (ROE)

Table IX reports results of the regression model 2 of firm performance determined by return on equity (ROE). The P-value is significant at the 5% level, indicating there is a relationship between the dependent variable and the predictor variables though R-squared is low at 0.013. The regression estimates show a positive and a 10% level of significance of the relationship between ACQ (acquirer/ target) and the firm performance (ROE). For the Cross border M&A deals and Domestic M&A deals(CB) variable, the regression estimates a positive and significant relationship between the independent variable and firm performance, so this indicates that for every 1% increase in domestic M&A deals there is an increase in ROE at a coefficient of 0.162213.

The regression coefficient shows a negative and insignificant relationship between firm size (SIZE) and firm performance, which indicates that for every percentage increase in firm size, firm performance decreases by a coefficient of 0.027. This results do not support our assumption that firm size is positively related to firm performance. The regression estimates on relationship between leverage (TDA) and firm performance shows a positive and insignificant relationship which indicates that increasing leverage by one percent increases firm performance by a coefficient of 0.081. Although we did not make any predictions regarding the impact of leverage on firm performance, our results show that increasing leverage most likely will result in a gain of firm performance.

5. Discussion of Results

According to our present results, our study confirms the notion that M&A improve firm performance. The findings further indicate that cross boarder M&As are less effective in terms of improving firm performance as compared to domestic M&As. The implication of such findings is that in times of recession, firms should look at merging as the best alternative solution to remain alive than opting to wait for their death. In East Africa, mergers within are more effective as compared to those of cross border. Firm performance was operationalized entirely using CAR and ROE. Whereas firm size as a control variable has no significant relationship with ROE, it has a significant relationship with CAR. Further, leverage is insignificant with CAR and a weak positive relationship with ROE. This study's results suggest that the method of payment has a negative and an insignificant relationship with CAR and this implies that majority of the acquirers in our sample favour other methods of payment over stock based deals.

Our study results confirm results of previous researchers such as Gugler et al. (2003) who examined and evaluated the effects of mergers and found that profitability is positive in all five years after mergers and is significant in every year at 10% level. Also, Ndung'u (2011) studied the effects of merger and acquisitions on financial performance of commercial banks in Kenya and

found that there was an improvement in financial performance after the merger. In the East African region, firm mergers within partner states (Uganda, Kenya, Tanzania, Rwanda and Burundi) are much more effective than the mergers between firms in East African region and those outside East African region in terms of improved firm performance. This can be attributed to the fact that firms within the East African region operate under similar conditions for example they source their customers from the same pool and the customers' cultures are almost similar or related. A Ugandan may find it easier to consume products manufactured in Kenya than those from say Ethiopia.

Whereas a number of researches have been carried out on firm performance, this study provides an initial empirical evidence on what really matters for firm performance especially during the period of economic recession where there is low purchasing power as witnessed by low sales and corporate collapses. To hedge against such corporate collapses, it is important that firms consider merging with emphasis on mergers within the East African region (community). Domestic mergers and acquisitions are more helpful in improving firm performance as compared to cross border mergers and acquisitions. Abnormal returns are expected to remain stagnant at the announcement date in most times and will immediately raise after the announcement (Window 3). This finding is in line with the findings of Mushdzhi & Ward (2004) who reported that South African acquiring firms' shareholders lost approximately 0.55% which was significant around the announcement dates. Further, Smit and Ward (2007)'s study that used a sample of 27 firms found that acquiring firms in the same country neither earns significant positive abnormal return nor negative abnormal return in the short run. Barde and Salisu (2015) observed that merger and acquisition announcements have no impact on shareholder wealth in the short run. So, abnormal returns are mostly realized after the M&A announcement dates and not before or even during the announcement dates of M&A. The domestic M&A firms perform better than cross border M&A and this could be attributed to by possibly the East African community bloc. Management of various firms within the East African bloc may then take advantage of the bloc by carrying out M&A activities in the region to increase on the economies of scale and economies of scope.

In terms of control variables, it really matters whether the mode of payment is by cash or by other means say shares. Cash deals are more preferred as compared to other mode of payment. Firms in the M & A deals are more interested in increasing their liquidity to be able to meet their day to day obligations. Firm size only matters in improving CAR whereby, larger firms may register higher CAR after the M&A than smaller firms and this concurs with Moeller, Schlingemann & Stulz (2004) who found a strong evidence of a size effect in the acquisition announcement returns. Leverage has an association with ROE but this also minimal and thus for the East African region, leverage has little to do with firm performance after M& A deals.

6. Summary and Conclusion

This study aimed to find out whether there is a significant impact of M&A on firm performance. This was achieved through an event study of 330 observations with 234 completed deals in East Africa using the dataset obtained from zephyr database and Thomson one DataStream for a period of 2005 to 2015. The two M&A activities we examined; Acquirer/ Target and cross border M&A deals/ domestic M&A deals. M&A performance is measured as the cumulative abnormal returns (CAR) of (-1,1) event window. Firm performance is determined using the accounting measure of return on equity (ROE). This research involved a two-step procedure. The first step entailed an event study concerning the abnormal returns earned by the acquiring firm's shareholders. The second step included two regression models that is (1) the CARs and independent M&A activities and (2) the firm performance variables and the M&A activities. In both models we used control

variables which we found significant in other studies. For all firms, only one transaction within one year is allowed in the sample. Target firms must be in East Africa (Kenya, Uganda, Tanzania and Rwanda). Firms from all sectors were included to increase our data sample. Model 1 is significant at a 10% level confidence of the regression and appears the best to explain M&A performance. The results from the regression measure of M&A performance estimates a negative and significant relationship between the acquirer returns and M&A activities. We also find a positive but insignificant relationship between domestic M&A deals and M&A performance (CAR). Model 2 is significant at 5% level of the regression to measure firm performance. The results from the regression measure of firm performance estimates a positive and significant relationship between the ACQ and firm performance. We also find a positive and significant relationship between domestic M&A deals and firm performance (ROE). Comparing both regression models, we conclude that the acquiring firm shareholders' wealth is reduced around the announcement of M&A though it increases the return on equity of the acquiring firm. Furthermore, the domestic M&A deals have a higher ROE which means the domestic M&A deals increase firm performance than the Cross-Border M&A deals in East Africa.

This study makes important contributions in the following ways. First, the exact mechanism through which firms can improve their performance especially during the time of recession is found. In the presence of an opportunity to merge or even acquire another firm, firms may explore this and survive in the future. Second, since there is limited literature on the effect of M&A on firm performance in the East African countries, this study becomes important in terms of its literature contribution to the already existing literature. Finally, this study is of value to the East African Community in regards to evaluating its objectives on regional economic growth through M&A influence and also drive positive business and logical decisions on M&A activities in the East African region.

Like any other study, this study is not without limitations. The private owned firms do not publicly show/share their financial statements due to their nature of operation. This made the collection of data difficult as well as time consuming thus resorting to using the publicly traded firms (target firms in the East African States) for our study. In addition, it was hectic to collect data on all the publicly traded firms that have under gone M&A in East Africa since some firms lack financial data in DataStream and our focus was on secondary data and by that, we had to exclude those firms from our data sample and yet if their data was available it would have increased our data sample thus having unbiased conclusion. Further research could be done on the impact of corporate governance on the M&A performance of firms for both private and publicly traded in East African region. More so, research on the effects of cross border merger and acquisition of firm performance using evidence from East African region is necessary so as to obtain more insights into the contribution of foreign investment in the region. Nevertheless, this study' results remain useful.

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